Diageo North America President's Call with Debra Crew

Transcript including Q&A - Monday 16th November

Debra Crew:

Good morning I'm Debra Crew. And I am delighted to be here today to have the chance to introduce myself to many of you who may not know me. I joined the Board of Diageo just over 18 months ago serving as a Non-Executive Director and was impressed by what I saw. So much so that when Ivan offered me the opportunity to become more involved in the company, I jumped at it. So when Dierdre retired at the end of June, I stepped off the Board, and I became President of Diageo's North American business. As you can see from my background I have spent my career working in the consumer products industry. Most recently I was President and CEO of Reynolds American and prior to that I had roles at PepsiCo, Kraft, Nestle and Mars. Despite joining in such "unusual times" I have truly enjoyed my first four months leading the North American business and I have been able to, at least remotely, get to know our people, our distributors and customers, and other key external partners.

I am both humbled and proud to lead such a talented and dedicated group of Diageo associates particularly in the face of such a challenging operating environment over the last few months.

I want to use today's presentation to:

- Give you my perspective on how I see the US market opportunity
- Share my first impressions of Diageo's North American business
- Set out my plans for emerging stronger from this crisis. I'll focus mainly on the US and Spirits given its size and scale.

As you know from our AGM Statement at the end of September, our US business has been performing strongly in fiscal 21, and ahead of our expectations. We are scheduled to provide our next update on our fiscal 21 performance at our interim results in January.

The US total beverage alcohol market is large, around $170 billion, and it's growing. Growth is being driven by favourable market demographics and a strong premiumisation trend. You can see from this chart, that for the last decade, the spirits category has been consistently growing faster than beer and wine, increasing its share of the TBA market from 32% in 2010 to 39% in 2020. Despite this trend, spirits penetration remains relatively low. According to the latest data from Numerator, household penetration in the US is at 54%. This compares to 67% for wine and 75% for beer. Which creates an exciting opportunity for our business. In 2020, household penetration for spirits has increased at nearly three times the rate of beer, and two times the rate of wine. This trend has accelerated during Covid-19 as people moved more of their consumption of alcohol to 'lower tempo, at-home occasions', including 'cocktail-making at home' and enjoying spirits 'with food' more frequently. Diageo's household penetration has been increasing steadily over the last five years and we are incredibly proud of the fact that nearly one in three US households has purchased a Diageo product during 2020.

Over the last decade, the US spirits market has been consistently premiumising. The growth of 'premium-plus' price tiers has been out-pacing the growth of the standard tier, and the value segment has been declining. The tier that has been gaining significant share of spirits is 'super-premium plus' and you can see that trend has continued during Covid-19. The 'super-premium plus' tier has reached approximately 47% share of the US spirits market in 2020

You can see from the chart on the left side of this slide that the US market continues to be very resilient during Covid-19. In part, this is due to the structure of the US market. Even before Covid-19, approximately four out every five drinks were being purchased in the off-trade channel. Growth in the off-trade channel accelerated when bars and restaurants were closed and this growth has remained strong. Even as the on-trade channel partially re-opened, you can see the overall US Spirits market grew strongly during the first quarter of fiscal 21. In the first couple of months of Covid-19, we did see that the on-trade channel closure caused a slowdown in price/mix growth in Q4 of our fiscal 20. This was the effect of an adverse channel mix, combined with some ‘pantry loading’ of larger size bottles in those initial weeks of lockdown. However, you can see that premiumisation has since recovered, and accelerated above pre-Covid-19 levels during the first quarter of fiscal 21. And, we would expect this long-term trend to continue in the US Spirits market.

You can see from the charts on this slide, which shows data to end of calendar year 2019, that younger-adult, multicultural consumers are driving growth in the US spirits market. And this gives us a natural tail wind for long-term growth. Over the next five years, more than 80% of the growth in the legal drinking age population in the US is set to come from multicultural consumers. More than ever, we’re seeing this diverse and younger-adult cohort of consumers coming into our brands, both into our ‘new to world’ brands, as well as into our long-established brands, that have unrivalled heritage and provenance. This is particularly true for many of our fastest growing brands, such as Casamigos and Bulleit, which over-index with younger-adult, multicultural consumers.

Despite being the market leader in US Spirits, Diageo today has only 6% of total beverage alcohol share in the US. This shows a significant growth opportunity for our business over time.
You can see from the chart on the right that our spirits portfolio has been taking TBA share in recent years and we expect this trend to continue.

We take a disciplined approach to portfolio management. In the last few years, we have made a number of disposals, including Bushmills Irish Whiskey, our US wine business and 19 brands that we sold to Sazerac. These actions enable us to focus on our premium-plus brands and increase our presence in fast growing categories. We are also delivering our premiumisation strategy through acquisition. This includes Don Julio and Casamigos in the super-premium tequila category, and most recently Aviation in the super-premium gin category.

What I see as another real strength of our US portfolio is our impressive breadth and scale across categories. These charts also show that the mix of our portfolio has significantly changed over the last five years. As an example, North American manufactured whiskies are now larger than vodka and rum combined. Our investment in the tequila category has been another key growth enabler in recent years. In fiscal 20, organic net sales of Don Julio grew 26% and Casamigos grew 68%. The strong performance of these brands has established tequila as a significant category within our portfolio. US whiskey, Canadian whiskey and tequila are three of the fastest growing categories in the US and we see an exciting runway for further growth.

Diageo is the largest whiskey company in the US, with 22% share of all whiskey categories. Our portfolio is also one of the fastest growing, growing at a compound annual growth rate of 9% in the last two years. This reflects consistent and effective A&P investment, supported by strong innovation. Crown Royal is a great example of our success in using consumer insights to consistently build brand equity and launch new, incremental variants. We've been successful in recruiting new legal-drinking-age consumers and taking the brand into new occasions. Importantly our whiskey portfolio has increasingly broad consumer appeal, over-indexing to younger-adult and multicultural consumers versus TBA. As examples:

- Crown Royal over-indexes with African American consumers
- Bulleit over-indexes with the 25-44-year-old consumer

- Buchanans also over-indexes with that age cohort, in addition to having a strong Hispanic consumer base
- And Johnnie Walker over-indexes with Asian and Hispanic consumers

Diageo has the fastest growing tequila portfolio in the US. While we are still a small player, with only around 10% of category share. This offers an exciting opportunity for future growth. NABCA shows our tequila brands growing at a compound annual growth rate of 43% over the last two years, which added 320 basis points of market share. We continue to invest strongly behind Don Julio, Casamigos and DeLeon. And are excited to be adding the Astral tequila and Sombra mezcal brands that were recently acquired as part of the Davos acquisition.

Our focussed investment in A&P, innovation and M&A has established a strong portfolio of 'premium-plus' priced brands – which reaches across multiple categories. There are some great examples on this slide. I see the strength of our innovation capabilities as a real differentiator for our business. It has been a key enabler to recruiting and re-recruiting consumers into our portfolio. Great examples of our successes in recent years have been Crown Royal Regal Apple, Vanilla and Peach, Ketel One Botanicals and White Walker by Johnnie Walker. Innovation will remain a key growth driver and later in the presentation I'll give you a preview of some our fiscal 21 launches. It's important to note that many of our fastest growing variants today like Crown Royal Regal Apple and Bulleit Rye are innovations we developed.

You can see from this slide that we have built a portfolio that is well-balanced for sustainable growth. Our 'core' brands, which include Crown Royal, Smirnoff and Captain Morgan, make up around 55% of our sales and in aggregate, have been growing at a CAGR of around 4.6%, slightly below the overall spirits market growth rate. These large and high-volume brands are really the engine of our business and support our operating leverage. Around 40% of our sales come from our 'growth' brands, such as Don Julio and Baileys. In aggregate, these brands are growing significantly ahead of the US market and really drive our share and top-line growth. The smallest component of our sales comes from our 'nurture' brands. While these brands, such as Roe & Co and George Dickel, are small contributors to our business today they fit into dynamic areas of spirits category growth. We expect the investment we are making now and in the coming years, to build these brands to be the next generation of growth drivers for our business.

We have seen significant acceleration in the growth of Diageo Beer Company since 2017. This reflects the rapid growth in the US total malt market over that time and Nielsen shows that both our Guinness and Smirnoff RTD portfolios have successfully gained share in the off-trade total malt market over that period. We have driven this through increased investment behind A&P and innovation. Our consumer-led innovation has responded to two seemingly contradicting trends 'holistic wellbeing' and 'indulgence'. The launch of our Smirnoff Spiked Sparkling Seltzer range was a response to consumers looking for a lighter choice. While our Smirnoff Ice Smash range responds to consumers wanting to also enjoy indulgent adult treats. These brands, which were launched in 2017, have been extremely successful and they now account for a significant percentage of total Diageo Beer Company net sales value. We have significantly grown our presence in convenience stores and large chains, which have become increasingly important channels during Covid-19. We have won retailer trust and expanded convenience facings by 19% and chain facings by 9% in the three months to October 2020, compared to the same period in 2019. Our Seltzer, Smash, and Red White & Berry innovations all remain in double-digit growth after several years in market.

I'm sure at least a few of you are wondering how Covid-19 has impacted our overall ambition, investment strategy and portfolio priorities. Our global performance ambition for Diageo hasn't changed we want to be one of the best performing, most trusted and respected consumer products companies in the world. And we have six strategic priorities that will enable us to achieve this. As Diageo's largest market, North America continues to be critical for performance delivery. With all of the opportunity and resilience we are seeing in the US market, we want to ensure our business emerges even stronger than it was before Covid-19. We are building on the strength of our portfolio and putting strong A&P investment behind our brands. And of course, we want to do so smartly. Having worked in a number of other consumer goods companies I have been so impressed by the technology tools and the data we have at Diageo North America. We are leveraging the investments we have made over the last few years. For example, with more consumers staying at home, we are using data and tools to deliver targeted messaging to consumers via social media, down to the zip code. We combine this targeted messaging with data from our platforms such as EDGE to inform our activations at a store level to win in the most critical outlets. We are strengthening our position in the off-trade channel, where shoppers are buying today, while also increasing investment in the fast-growing e-commerce channel. These investments, combined with our ongoing commitment to do business in the right way, will position us to deliver sustainable growth.

As many of you might remember from the NAM President's call this time last year, Deirdre talked about investments we had made in technology that were enabling us to identify emerging consumer trends to inform our brand strategies. This was certainly helpful as we saw the impact that Covid-19 had on consumer behaviour. This slide gives a flavour of the key consumer trends we've been seeing in recent months. While we saw some aspects of this pre-Covid, the trend of at-home occasions becoming more informal and spontaneous has accelerated. More than two-thirds of drinking occasions are spontaneous, up 10% since the start of the pandemic. An increased desire for convenience has been another key trend, in particular the demand for pre-mixed cocktails, cocktail kits, cans and e-commerce. Before the pandemic, less than 1 in 3 alcohol drinkers were even aware that they could buy alcohol products online. Contrast this with July 4^{th} this year when 1 in 3 alcohol drinkers used an e-commerce platform to buy alcohol online. Consumers have been increasingly seeking reward and indulgence in recent months. In recent research, 40% of drinkers believe that this holiday season they expect to 'splurge more than they normally would' on alcohol for themselves or others in their household. 'Gifts for others' also scored 40%. These percentages were higher than the scores for things like 'entertainment', 'decorations' and 'travel'. Finally, there is no doubt Covid-19 has a profound effect on communities. Consumers across North America have seen their neighborhood businesses and on-trade venues threatened. They are figuring out how to sustain all areas of their lives, from careers, to family, to lifestyle, to relationships. Our socially conscious activations are more than just the right thing to do in the moment, we see these as opportunities to build on our long-standing partnerships with the key custodians of our brands on the front-line, bartenders, small businesses owners and artists.

In the context of the four key consumer trends that I've just highlighted, I'm now going to share a short video. I think it really brings to life how our brands have responded to the changed needs of consumers in 2020 and how we successfully pivoted our marketing activations.

As I mentioned earlier, innovation has been a key driver of growth. We will continue to use innovation to reach more consumers, in more occasions. We are really excited about our pipeline for fiscal 21 and there are some fantastic examples of recent and upcoming innovations on this slide. You can see that we are really expanding our portfolio of ready-to-drink offerings. This includes ready-to-drink cocktails across our Tanqueray, Crown Royal and Ketel One brands, which meet consumers' increased desire for convenient drinks in a portable format. In early 2021, we are launching Guinness Nitro Cold Brewed Coffee, which marries the magic of Guinness nitro with trending coffee culture in lighter, brighter drinking occasions. We are continuing to drive innovation across our other well-known brands including limited editions to celebrate the 200th anniversary of Johnnie Walker. Our recent launch of Captain Morgan Apple Slice has had a terrific reception from consumers and our seasonal LTO, Baileys Apple Pie, was the number one innovation in NACBA in September. We are excited to be launching 'Baileys Deliciously Light' in January, which has 40% less sugar and calories than regular Baileys, but still tastes delicious, so you won't be missing out!

The e-commerce channel for TBA in the US has historically been very small mainly due to regulatory restrictions and low consumer awareness. Covid-19 has really increased consumers' awareness of the channel and their comfort in using it, and as a result, there has been a significant acceleration in on-line demand for TBA. Drizly, the leader in alcohol e-commerce and delivery, has grown over 350% in 2020 compared to 2019. Drizly predicts that 20 percent of off-premise alcohol purchases will be transacted online within the next five years, compared to less than 2% in early 2020. For the last few years, we have been investing to build our capabilities in this channel and we have been establishing key partnerships that ensure our brands are well positioned. We have more than doubled our A&P investment in e-commerce in the last 18 months and increased the number of people working in this channel. Our e-commerce business has a more premium mix of brands and the rate per case is typically 15-25% higher than our business in brick and mortar. E-commerce consumers tend to be younger-adult, more urban and very interested in discovery, which lends towards whiskeys, tequilas and higher-priced products. Where we have data, our market share in this channel is 2 to 3 percentage points higher than our share in the 'brick and mortar' channel. We will continue to invest strongly behind the e-commerce opportunity, and I believe we have the right capabilities and portfolio to win in this emerging channel.

Prior to Covid-19, we had been continuously increasing our investment in A&P both in absolute dollar terms and as a percentage of net sales. We reduced A&P investment in the second half of fiscal 20, when it wouldn't have been effective. However, we are recovering to accelerated investment levels in the first half of fiscal 21, as consumer demand has strengthened, and we expect to see an effective return. We benefit from tools such as Catalyst in ensuring we invest with the most effective and efficient marketing mix to support growth. We will also continue investing behind our capacity requirements as growth accelerates and of course, we will do that in a way that supports our sustainability agenda. You may have seen the recent announcement regarding the new Bulleit distillery we are building in Kentucky, which will be one of the largest carbon-neutral distilleries in North America. Finally, as I have already mentioned, we are investing in smart brand acquisitions. As we develop our portfolio over time, we will continue to look for opportunities to acquire fast-growing brands in exciting categories.

We recently celebrated the conclusion of our highly ambitious 2020 Sustainability and Responsibility Goals. Our 2020 targets were selected to align with the UN's Sustainable Development Goals and designed to cover Diageo's three main focus areas:

- Reducing our environmental impact;
- Building thriving communities; and
- Promoting positive drinking.

Some of our key achievements by 2020 were:

- Halving greenhouse gas emissions across our business, globally a 50% absolute reduction;
- Improving water efficiency by 46%;
- Having over 99.5% of our packaging now recyclable;
- Empowering 435,000 women through our community programmes; and

- Reaching 2 million people with moderation messages from our brands.

We will be announcing the new Diageo targets to 2030 at the end of this month.

Promoting positive drinking is fundamental to our business at Diageo and an essential part of our performance ambition. In North America, we've already done work in this area, including Crown Royal's 'Water Break' campaigns, which most recently, were promoting responsible drinking during the NBA Playoffs and in the NFL Kick-Off game. This month we are re-launching DRINKiQ in North America, which now provides information to support the reduction of alcohol harm.

We're also very proud of our inclusive and diverse culture. However, there is always more work to do, and we continue to improve and advance our programmes. Globally, at the end of fiscal 20, 39% of leadership roles were held by women, taking us beyond the target we had set for 2020. 55% of our Diageo Board members are women and 38% of our Executive Committee are women. The North American Executive team that I lead, is composed of 50% women and is 20% ethnically diverse. You may also notice many of our brands are actively supporting inclusivity and promoting diversity in our industry and culture. In June, we announced a $20 million "Diageo Community Fund" to help address the disproportionate social and economic impact of the pandemic on Black communities and businesses. In August, the Guinness Open Gate Brewery in Baltimore introduced the beer, Black is Beautiful. It was created by Weathered Souls Brewing and it is a collaborative effort amongst the American brewing community and its customers to bring awareness to the injustices that many people of colour face daily.

Our new carbon-neutral distillery in Lebanon, Kentucky, which is expected to be fully operational in 2021, will be powered by 100% renewable electricity. We are really proud that Diageo has created the world's first ever 100% plastic free paper-based spirits bottle, which we announced at the start of fiscal 21. The bottle is made entirely from sustainably sourced wood and will debut in early 2021 with Johnnie Walker. Here in North America, we are also contributing to packing sustainability, having recently removed virgin plastic from Seagram's 7 Crown bottles. From the end of June, these new 7 Crown bottles, made from 100% recycled plastic, became available on shelf. The move is a first for the brand and for Diageo and will reduce the use of virgin plastic by almost 1,000 tonnes annually.

Diageo North America is such an exciting business to have joined. Spirits is a vibrant and growing category, and as the market leader, Diageo is playing a key role in shaping and driving that growth. As you have seen from today's presentation, we have a portfolio of leading brands, supported by best-in-class marketing capabilities and a strong innovation pipeline. Most importantly, we have a team of people in Diageo that have the talent, commitment and energy to really drive our business forward. This is powerful combination that I feel confident will enable us to emerge even stronger from this crisis and deliver long-term growth.

I want to leave you with another short video, which demonstrates the agility of the team I lead. It's from our US beer company, which arguably had to overcome the biggest challenge during Covid-19. Guinness has historically relied heavily on a robust on-trade channel, particularly on St Patrick's Day. This team's pivot has been incredible and inspiring for all of us. Thank you all for listening and I look forward to answering your questions shortly on our live Q&A call at 8am EST or 1pm GMT.

Q&A call with Debra Crew

Operator:

Good morning and afternoon. Welcome to the Diageo North America President's Q&A Call. This is a live Q&A session for 30 minutes following the prerecorded presentation uploaded earlier today to diageo.com. Today's conference is being recorded. Your call today will be hosted by Diageo's North American President, Debra Crew.

To ask a question please press star one on your telephone keypad. Please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star one to ask a question. We are now ready to start the call. Our first question comes from Simon Hales from Citi. Please go ahead.

Simon Hales:

Thank you. Hi Debra, hi everyone. Congratulations on your new role, Debra. Thanks for the presentation today. I had a couple of questions, please. You highlighted, obviously, in your presentation, and we've seen this clearly the acceleration of the premiumization trends during 2020 as COVID has hit, especially in that super premium plus segment. How are you thinking about what happens when we get into 2021 and perhaps we start to lap in calendar Q2 those acceleration in trends and consumers perhaps have other alternatives once again to spend their disposable income in terms of other leisure or social activities? Do you think you're going to be able to sustain the level of penetration and premiumization growth that we've seen? So just a broad question around that. And secondly, can I ask you about stock levels now in the U.S.? You've clearly seen some stock replenishment at the wholesaler level in fiscal Q1. Has that continued at all into the second quarter? And I appreciate this bit a little bit difficult to answer, given it varies by brand and geography. But broadly, where do you think inventory levels are now within the wholesale chain compared to this time last year?

Debra Crew:

Great. Thanks, Simon. So I'll start with the premiumization question. And I think you would have seen from the chart this morning, this premiumization trend has been going on for a decade. So certainly, COVID at the very beginning of COVID, we had a couple of months where we didn't see that premiumization, but then it quickly sort of went back on course. So we would expect that trend to continue as it has been and, in particular, in that kind of super premium area.

As far as when you start to lap and different things are going on with consumers, one of the things that we're seeing is that consumers are wanting to drink better, not more, but drink better. And so we think that's just an ongoing consumer insight, and that is going to continue to drive those premiumization trends.

As far as stock level, what I would say is we've seen a modest level of restocking at the retail level. But recognize, if you look at Nielsen trends and other sort of public data sources that are out there, I mean, demand is really strong right now.

Simon Hales: Got it thank you.

Debra Crew: Great, thanks.

Operator:

Thank you and now we'll take our next question from Olivier Nicolai from Goldman Sachs. Please go ahead

Olivier Nicolai:

Hi, good morning Debra. Just got 3 questions on my side, if I may. First, could you give us a bit of an update on the on-trade channel today? Are we running at, let's say, 50% of where we were a year ago? And as the on-trade reopens progressively in 2021, do you expect the off-trade growth to slow down substantially? Or do you think that some of that shift from on-trade to off-trade will stay? That's the first question.

Second question is actually more a follow-up on one of your slides why you talk about the level of household penetration for spirits. Is it realistic? I think you mentioned the number, which was 54%. First, where was it 10 years ago? And is it realistic to get the same level of penetration for spirits than you have for beer, which I think is about 20 points higher?

And just a last question on your brands. Johnnie Walker is perhaps not performing as well as the rest of the whiskey portfolio. Could you just perhaps remind us what the key demographics are for the brand? And what's next for Johnnie Walker after that Game of Thrones extension, which was successful, but that was, I think, a couple of years ago now? Thank you.

Debra Crew:

Perfect. Yes. So let's just start by talking about the on-trade, I think, first. I mean look, what we're seeing, and it really is different state by state. And in fact, it's actually changing probably by the minute as we're talking. Because certainly, some states are - they're putting in curfews. We do see some states actually closing some of the indoor kind of dining and that type of thing.

So I would say it ranges anywhere from you have some states, I think, in fact, I just was reading something this morning. Texas is only down around 10%, so that's probably a state doing really well in on-trade. And then you've got some that are still down 60% of what they were. So you really have a kind of different environment out there depending upon where you're at. All of that being said, one of the things that we have learned during COVID is that as these things trade, as you see the on-trade closures and that type of thing, those occasions are simply moving home. So we're not really seeing a big impact to our kind of business as we're seeing that on-trade shut and then those occasions are coming home.

So I think, as we are looking at it, we're trying to support on-trade as it opens, and we're also trying to make sure that we're investing the right level of off-trade to kind of keep all the channel opportunity for us open as well as don't forget e-commerce in this as well, which is also - it's still small, but certainly growing. So we're seeing a lot of movements of these occasions, but it doesn't really change necessarily what we're seeing on our net sales.

I think you asked about household penetration. I have to get back to you on what it was 10 years ago because I'm not sure I've got that at my fingertip. And I'm not sure exactly what we even have going back 10 years, but we can certainly get something for you. But I will say what we have seen is continuing to grow. And could it get to beer? I mean look, it is growing faster. And I do think that as consumers get a kind of a stock level in their house, along with mixers, absolutely. You could change out those occasions, and I think that's how we're thinking about it. So we're looking at one of the reasons we're starting to look at our share on a total beverage alcohol basis is anytime anyone wants an alcoholic beverage, we would like them to consider Diageo and we want to be part of that equation.

I'm just getting a note from someone here with me. So it looks like in the last 5 years, we do have data going back to the last 5 years, it was between 28% and 32%[1]. So kind of in that, call it, 30%. So you have seen a really fairly large uptick in spirits over the last 5 years.

Finally, on the Johnnie Walker question. Look, we definitely had a tough year in fiscal '20 on Johnnie Walker, mostly because we were lapping the Game of Thrones White Walker, which was incredibly successful for us. And then also the closure of on-trade really impacted that brand more so than some of our other portfolio.

That being said, what's next for us on demographics on Johnnie are actually very positive from when you look at sort of the appeals of Hispanic consumers, Asian consumers. These are 2 kind of growth demographics in the U.S. and both have over-indexed on Johnnie Walker, so we feel great about that. It is right now, the core of the business is a little bit older cohort. And one of the

[1] *Diageo Portfolio Household penetration went from 28% CY16 to 32% 12mths ending 30/09/2020. Household penetration for Spirits was 50% in CY16, source Numerator*

things that we're really doing is we want to increase our relevancy with that younger legally drinking age kind of consumer, that 25 to 44 year old. So we've got a lot of activity. Hopefully, maybe you even saw, if you happen to be watching in the U.S. election night, we had a new ad that was launched - that launched on Johnnie Walker, really trying to get the Keep Walking tagline kind of reestablished in the U.S. It was Brittany Howard from Alabama Shakes singing You'll Never Walk Alone. So great song, really appropriate for 2020 but really a great way to bring Johnnie Walker part of the conversation for today and bring real relevancy.

And I should add, we're doing great on Johnnie Walker on the higher marks. So Johnnie Walker Blue, Johnnie Walker Black doing extremely well. So we really feel great, and we're seeing really nice retail sales trends improving, and we do see share sequentially improving as well. Thank you.

Olivier Nicolai: Thank you very much.

Operator:

And now we'll take our next question from Sanjeet Aujla from Crédit Suisse. Please go ahead.

Sanjeet Aujla:

Hi Debra, a couple of questions from me as well. Firstly, I recall in Q4 for F20 (inaudible) Diageo lost of share of spirits. How has market share evolved in the last quarter [as] the industry has accelerated? And my second question is just on A&P. You spoke a little bit at the end about stepping up A&P levels. Is it reasonable to assume A&P now starts to run ahead of NSV after growing below NSV last fiscal year? Thank you.

Debra Crew:

Yes. So Q4, we definitely see sequential improvement on spirits. What we are seeing that we're very excited about as well is we are gaining share in total beverage alcohol. So we are seeing really improvements across the board, and we feel great about that.

On A&P, look, A&P, we're definitely reinvesting as we're seeing the increase in consumer demand. We've been on a trajectory of this really since 2017, continuing to try to build back our A&P level. And really, the only time we pulled back was at the beginning of COVID. We really kind of zero-based our A&P, as you would imagine, and really, relook everything we were doing. We had a lot of money that was going towards sampling and experiential. Frankly, things that just weren't kind of pay out because we did cut our A&P in that second half. But as we've seen demand come back, and as we're seeing opportunity, we are definitely putting back our A&P levels.

Operator:

We'll take our next question from Rob Ottenstein.

Robert Ottenstein:

Okay. Well, maybe because I'm closer, calling in from New York. Look, first of all, congratulations, and welcome to the team here. Traditionally, a lot of presentations for Diageo North America have spent some time talking about the competitive advantage of your route to market in North America and your distributor relations. I was wondering if you can kind of maybe give us an update on where that stands, what may be new or different that you're doing with the distributors in the U.S. as opposed to in the past, where things look in terms of their inventories and the whole sort of trade-off between sell-in and sell-out that you've been engineering over the last few years? Thank you.

Debra Crew :

Sure. Thanks, Rob. So yes. I mean we didn't mention that it was kind of getting to be a long video. We couldn't talk about everything we were excited about. But clearly, we do still see it as a competitive advantage, our route to market and our distributor relationship. In particular, I mean, you can't think about COVID and sort of the stresses that put on the system, but we do feel really great about our ability to respond to what was occurring, and that is really in large part to those relationships and how we were able to get through the various shifts that occur from on-premise to off-premise even as we're kind of things are going back and forth, as you would be aware, being in New York.

So we do feel great about those relationships. And what I would say is what's new and different? I mean you would have seen some of our route-to-market change in New York, which we actually were able to execute really well in the middle of all of this. And so -- and we do feel great about where we're at with all of our distributor partners.

As far as inventory, this comes back to, we've got a lot of data now in the system and we are able to very quickly respond in a very agile way to that. So we have not seen outsized sort of inventory buildup in different things, which you might expect as you're trying to do all the shifting. been able to manage that extremely well. So I think, as I mentioned earlier, we've seen a modest level of restocking at retailers. But given the strong demand and given how kind of close and we're playing this with distributors, we don't have outsized inventory sitting anymore.

Robert Ottenstein:

Is it, in fact, maybe the reverse for Crown Royal and some other brands? At least we read that, that a lot of retailers are actually having a hard time getting some key products.

Debra Crew:

Yes. I mean we've really had incredible growth on Crown Royal for the last 6 to 7 months, well above what any forecasts would have had for us. And so absolutely, we've had to manage that going on kind of an allocation process just to make sure that we get the Crown through the system. And so that's one area. And I would say, tequila is another area, which I'm sure you've read or heard things about. That's another one that you could absolutely say that's running reverse.

Robert Ottenstein:

Thank you very much

Operator:

And now we'll take our next question from Richard Withagen from Kepler Cheuvreux.

Richard Withagen:

Good morning and good afternoon. I missed the part of the call but -- so if this question has been asked, sorry about that. But I have 2 questions, Debra. First of all, you became responsible for the U.S. since July. So in what areas of the business do you plan to step up efforts and allocate more resources? And then the second question I have is on in beverages in the U.S., a lot is going on with different growth rates in channels, different category growth rates. What do you think will be the biggest game changer in TBA in the next 5 years?

Debra Crew:

Yes. So -- and no, I haven't answered these questions, so thank you. So as far as for July and from since July and where have I kind of focused resources, I mean, a lot of this has been -- we're very focused on the here and now just given everything that we have going on. So we are trying to respond with agility across where we're seeing the opportunities.

So with that said, I would say, look, we're clearly putting more effort against the off-trade and e-commerce because that's really where we're seeing the growth right now. Hopefully, you saw from the video this morning, you see we've got a portfolio that's really oriented towards some very great growth areas. So U.S. whiskey with the Canadian whisky, tequila, these are all great growing parts of our portfolio, and we're really doubling down against that momentum.

And then, of course, we are continuing to - because in the off-trade, we're seeing such tremendous results, we are using tools like EDGE, which I think we talked a little bit about in the video. Certainly, you would have heard Deirdre talked about it in the past. We're using tools like this to really make sure that we can target down to the zip code. And given COVID is creating all these different situations across the country, something like EDGE really gives us a big advantage, and we're certainly putting resources behind that.

Also, you would have seen the M&A that we did with Davos, bringing Aviation into the portfolio. We're very excited about that brand. So we've seen opportunities for M&A, we're definitely investing there. And then you would have also seen some of the investments that we're making in supply chain, and that's been a big piece of making sure that we've got a good, efficient sustainable supply chain to support the growth we've got.

You've asked about what we see the biggest changer in total beverage alcohol in the next 5 years. We talked a little bit about things like e-commerce. That's something that with COVID - prior to COVID, I mean, nobody even knew you could get alcohol almost online. I mean it was only 1 in 3 of the consumers knew before. I think it was less than 2%.

And now you see Drizly, they're predicting things like more than 20% could be in e-commerce in the future. So you think about the opportunities that are there, that would certainly change things within the industry. Certainly, we're seeing - I already mentioned some of the categories that we're seeing a lot of growth on. I haven't mentioned things like cocktails to-go. Hopefully, you saw in our innovation, we see a lot of opportunity there. We think there's a big opportunity to kind of drink better, and it's on-the-go occasion and so ready-to-drink occasion. So we see a lot of opportunity there as well. So hopefully, that kind of answers the questions there.

Richard Withagen:

It did. Thank you Debra.

Operator

And now we'll take our next question n from Edward Mundy from Jefferies.

Edward Mundy:

Hi Debra, good morning, good afternoon everyone. You mentioned on e-commerce, your rate per case is 15% to 20% higher versus bricks and mortar. Is that because you're selling more premium SKU brands? Or is that because you're able to catch a greater share of the value chain? That's my first question. The second question is to what extent you think or you'll be willing to share what you think is your medium- to longer-term top and bottom line growth ambition for North America?

And then my third question is, you worked in a number of FMCG. You've been privileged enough to be both at the nonexec level and the exec level at Diageo. What do you think are the 2 or 3 things that Diageo could do to become an even stronger business in both North America and more broadly based on your exposure to broader FMCG?

Debra Crew:

Yes. So first, on e-commerce, you're exactly right. It really is about more premium SKUs. When you think about the buyer in e-commerce is sort of the younger legally drinking age kind of consumer that is a little more urban and they are looking for higher marks in brands. So it really is about more premium SKUs kind of driving that.

Look, as far as medium to longer term, I mentioned, we are very focused on kind of the here and now and really emerging stronger from this crisis because this is one of these moments that we really think consumers, if you think about your own life, you're just reassessing sort of everything. And so we think it is very important to come out of this stronger.

That being said, I think Diageo North America has had a terrific story over the last 3 to kind of 4 years of just this consistent delivery. And that's certainly something that I want to build upon because I think that's really important. We do see ourselves as providing kind of outsized growth within the broader group. And so that's something that certainly, medium to longer term, I would want to continue to grow on.

I've been super impressed by the tools that Diageo really have and has been building up these capabilities over the last several years, so there's been a lot of investment in. And I know looking back through prior presentations that Deirdre had talked with many of you guys about on the investments into Catalyst, into EDGE and Trax and there were all these tools. But I can tell you, it is truly impressive. And certainly, through COVID, it's been great to be able to come in and to leverage the insights there to be able to respond to the market situation and down to the zip code level. So great tool there.

And I would see that once we get out of this crisis, those tools are going to continue to serve us really well. I think between the insights, the innovation, the investment into marketing, I really see our ability to be able to accelerate growth from where we've been. I see us continuing to grow share in total beverage alcohol, and I'm seeing sequential improvement in spirits. So I mean I think that's probably as far as I'll go right now about I mean here, we don't have any guidance out here so I'll just leave it at that. But we really do feel great about the opportunities for the business. I think I answered all...

Edward Mundy:

And my third question. In terms of the things that you think that Diageo I mean, it's obviously a strong business, strong brands and good execution. But are there any areas that you think any gaps for Diageo to close as you look across both North America and the broad business based on your exposure to other FMCG?

Debra Crew:

Yes. Look, I don't think it's a gap per se. I just think it's really leveraging the opportunity with the portfolio that we have. So really doubling down behind places in the portfolio where we have momentum. I've grown up around things that I've been kind of relentlessly focused on share. And so certainly, that's going to be a focus of mine.

And I would say really getting out there with, if you look at what's going on with the consumer right now, there's a lot going on, I think, as these really emergent spaces for spirits are quite different for us, things like gifting, things like the ready-to-drink and all these areas that I think for spirits we haven't really gotten into that so much. So I think there's a real opportunity for those to create kind of more occasions for spirits than what we've had in the past.

Operator:

And now we'll take our next question from Trevor Stirling from Bernstein.

Trevor Stirling:

Hello Debra. So apologies if these questions were asked before. I got bumped off the call. Two things. One, if I look at the latest NABCA data, it looks as if in NABCA at least, industry volumes are growing roughly 10%, and price/mix is running at mid-single-digit plus. Do you think that represents the broader industry?

And the second question is, you understand we've talked on some of the great success stories in the portfolio at the moment, but a little bit less about Smirnoff and Captain Morgan that are still very significant brands. What do you think you can do to turn those around, but arguing maybe a little bit more tired in the lower growth part of the industry?

Debra Crew:

Yes. So you asked about NABCA data and sort of if that's more representative. I mean I think, look, and I mentioned this earlier, all of these states have a lot of different things going on. So I think that's probably about in the neighborhood of what we are seeing out there, recognizing that it can be vastly different sort of state to state. But I think in general, that's probably a good way to look at it.

And on Captain and Smirnoff, because we haven't talked as much about those areas, but I will say we are seeing, certainly on our vodka portfolio, we're seeing improvement there and we're now gaining share. On the latest Nielsen, we're actually gaining share of vodka. Now granted vodka is part of overall spirits is shrinking, but it's good for us to see. Admittedly, it's mostly on those premium marks of Ketel One and Cîroc are actually driving that share growth, although Smirnoff is sequentially improving. So but look, I mean, vodka, we certainly have opportunities there. And I think a lot of it is around innovation.

I think in the video, we did highlight some of our Smirnoff innovation that we've got coming the second half, which we're very excited about. Because I do think, with Smirnoff, it is about keeping really relevant and having some news and kind of talk value to it. And I think that's what's helped us. And if you go back and look in places where we've gained share on Smirnoff, it's usually when we've done really great innovation that connects with the consumer. And I should mention, Smirnoff -- on our Smirnoff Ice portfolio and on our malt beverage, Smirnoff is actually doing really, really well. So from a trademark perspective, we know that Smirnoff does work with that kind of younger legally drinking age consumer. We know it from the Smirnoff Ice and malt beverage portfolio. So I feel really good about Smirnoff.

Captain, look, Captain is still one of the top brands in the U.S., still has really broad appeal. And actually, this year, for 2020, actually, both Smirnoff and Captain gained household penetration. And I think that's during COVID, people wanting to return back to these big brands that they're familiar with and they know. And also, Captain makes great cocktails. Great, simple cocktails, which when people are making cocktails at home, that's what they're really looking for. So I think there's more opportunity there on just focusing on the great, I'll call them, yummy cocktail because they really are. We have to make some really great simple serve, and so we know that that's the way to go there. And we [have] been looking for, you'll be seeing some new kind of look and feel to Captain in the future as well.

Operator:

We have time for one last question. Our next question comes from Laurence Whyatt from Barclays.

Laurence Whyatt:

Hi, good morning, good afternoon. Thanks very much for the questions. I was wondering, the first one, just look at the cost savings that you're able to take out of the business towards the end of last fiscal year. And how much of those do you think you will be able to maintain as we emerge from the COVID situation?

Secondly, on your distribution cost, we've seen quite an uptick in cost of trucking, in particular, around the U.S. I'm just wondering if either the costs are going to impact you or the availability of trucking drivers? And have there been any logistical problems on the back of that increase in trucking costs?

And then finally, slightly different. Just drawing on your experience from Reynolds and as we talk to investors more and more, we're being asked about ESG-type credentials and obviously, the tobacco industry is largely removed from any fund that focuses on ESG. There are a few funds that are starting to talk about alcoholic beverages in the same light. And I was wondering what you think would be the best defenses for the alcohol industry when it comes to being a force for good in the world and in the world of ESG? Thank you.

Debra Crew:

Okay. So yes, I'll take the cost savings one first. So definitely, if you go back to fiscal '20, we did cut out some A&P. I talked about that earlier. So we reduced marketing by about 6%, and we had a reduction in other kind of expenses that really offset -- actually, we have lower fixed cost absorption and then we had an adverse channel mix. So that's kind of how our margins came together for fiscal '20. Clearly, without really providing a whole lot of guidance, but at the same time, I think you can think about this going forward, that some overhead savings will clearly continue as people aren't traveling this year yet. So that's one way to think about it.

Our fundamentals are strong. Premiumization is a long-term trend. We are seeing volume growth that drives operating leverage, so all of these are good guys. On the negative, I would say, we do have an orientation to invest. I've talked about A&P. We definitely want to continue to strengthen that because we know that helps to drive our top line and our share growth. So hopefully, that gives you a little bit of sense for cost savings and where we're at on margins.

As far as distribution, look, this is something that I mentioned earlier, there was someone who had asked about our relationship with our distributor partners. We do feel great about those relationships, and we are keeping close to make sure that we can get the loans we need and that we can get product out into retail. The industry is certainly seeing stress on supply and the costs on some of these lanes are certainly up. So we are managing through it, I would say. And I wouldn't expect sort of service interruption type of thing. We're able to deal with it.

Look, as far as ESG, I mean, ESG is super important. And I actually think Diageo does a tremendous job in this area. And I think things like promoting positive drinking is really important. We take that very seriously. That's not just talk to, that is something that we really, really do believe people should drink better, not more. And we have a lot of activity going on to make sure that we're trying to reduce the harm out there. The drunk driving, the binge drinking, the drinking under age, all of that, we make sure that we absolutely do everything we can to eliminate that because that's where you fall into the hole of having problems.

So look, I think we take that really seriously. The grain-to-glass sustainability, we also take really seriously. It is one of our 6 strategic objectives along with positive drinking. And we are trying to be a force for good on inclusion and diversity as well. So you'll be hearing more from Diageo on our 2030 targets, which I think are really bold. They're bold in the sense of even if you look across any other FMCG. So we're not just comparing ourselves to other players in the alcohol industry, we are really looking at goals that will set us apart across FMCG. So stay tuned for that. But yes, we do take it seriously, and we want to make sure that people know what we're going for there.

Operator:

Thank you. In the interest of time, this will conclude today's Q&A session. Ms. Crew, I'd like to turn the call back to you for any additional or closing remarks.

Debra Crew:

Great. Thank you for your time today and your interest in Diageo. Thanks.

Operator:

This concludes today's call. Thank you for your participation. You may now disconnect.