New Age Beverages Corporation NASDAQ: NBEV)
Investor Conference Call
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CODY SLACH:

Good afternoon…and thank you for joining New Age Beverage Corporation's first quarter 2018 investor conference call. I am Cody Slach with Liolios Group, the investor relations counsel for New Age. I'd like to welcome you all to the call today and to thank you all for joining.

On today's call we will have Brent Willis, Chief Executive Officer of New Age Beverages, Chuck Ence, Chief Financial and Administrative Officer, Michael Cunningham, Senior Vice President of the US Division, and Josh Hillegass, President of the DSD Division.

I'd like to remind everyone that this conference call may contain certain forward-looking statements reflecting management's current expectations regarding future results of operations, economic performance, financial condition and achievements of the Company. Forward-looking statements, specifically those concerning future performance, are subject to certain risks and uncertainties.

The transcript of today's conference call will be available on the Company's website, within the investor section at www.newagebev.com. I'd now like to turn the call over to Chuck.

CHUCK ENCE:

For the three months ending March 31, 2018, the Company delivered consolidated gross revenue of $12.8 million vs. $11.4 million in 2017, up 12%. Subtracting discounts and billbacks, at the net revenue level, the Company achieved $11.6 million vs. $10.8 million in the prior year 1st quarter. The Company started off particularly strong in the first part of the year with double digit growth in the first six weeks, but sales were negatively impacted by approximately $3.5 million due to working capital constraints, which severely constricted inventory levels.

Within our segments, most of the impact was felt in the US Division. The US Division is where we are launching all our new products at close to 50% gross margin, so the revenue impact also flowed through to our overall Company blended gross margin. The DSD Division, was up vs. prior year through February, but also felt the effect. This division was up 9% in January and was up 6% in February, but then was down 5% in March. Our International Division, that is becoming a much more significant contributor overall, was up 337% in January, 1,375% in February, but only up 19% in March…and the US Division was also up in revenue in January by over 60% before the inventory impact.

Despite the constraints, the International Division, the Ecommerce Division, and the Foodservice Division were all up triple digits in the quarter vs. prior year, albeit off of a smaller base.

Within our portfolio of brands…the Búcha brand continues to lead all brand growth. Our new initiatives, Marley Mate, Shelf-Stable Búcha, and Coco-Libre Sparkling, that importantly are all above a 40% gross margin are all showing tremendous growth and are all rolling out nationally in new distribution. As an example, one of our largest natural distributors was averaging one layer per week of Búcha sales in January. That's 1/6th of one pallet. Three months later, that same distributor is now ordering 12 pallets a week.

In gross profit, the firm delivered $3.1 million for the year vs. $2.9 million in the prior year, up 7%. Gross profit as a percent of sales, excluding shipping, was 26 versus 26% also in the prior year. Digging into what's behind this topline aggregate number however, its deceiving as January gross margin was 33%. With all of the shipping and incremental costs of goods sold experienced in the quarter as we were moving product around to cover inventory needs, this impact in the later part of the quarter brought down the gross margin for the full quarter to 26.4%, in line with 2017.

Total operating expenses for Q1 were $5.1 million vs. $2.9 million in the prior year. This increase was driven by a number of non-cash items including increased amortization on the almost $20 million dollars of intangible assets added to the balance sheet, stock option and stock expense associated with the acquisitions, and rent expense following our sale lease back executed last year. We still expect 25% of net sales OPEX expenditure as a good working model assumption for 2018. Versus our internal budget, our OPEX was actually right in line, but the impact to top line revenue from the working cap deficit, hurt us both in percent of revenue, and overall fixed expense absorption.

Adjusted EBITDA for the quarter ending March 31, 2018 was minus $1.3 million, stemming from the inventory shortfall to fulfill demand.

I'd like to now switch our discussion to financing and working capital. Given the planned growth in the business we knew we had an incremental working capital requirement of between 3 and 4 million dollars in the beginning of the year. We started work on that six months ago, and had the commitment for it to be in place no later than the end of January. It didn't happen, and we simply did not expect a delay in execution, but it happened nonetheless.

So, why has it been a challenge for the Company to put in place a simple line of credit, when we have a significant amount of current inventory and receivables over current liabilities? Let me try and explain it as directly and succinctly as I can.

Overall, we are swinging for the fences with the lowest cost of capital, as we always have. You obtain this…from the largest banks.. but this has a cost in time, in their processes, and their very big company ways of working. New Age had in this smallest quarter of the year, the 1st quarter, a borrowing base of between 8 and 9 million, of what is deemed by the banks as available inventory and receivables. Banks loan on about 70% of this – so that equates to around $6 million. Take from that $2 million for US bank and $1.5 million that we owe 12/31/18 to the Coco-Libre noteholders. That's the total debt we have on the firm.

But, then the major banks want $2.5 million to be held in “unaccessed availability,” leaving you with very little left for working capital. We may likely get there with PNC, as we are moving into our bigger inventory and receivables quarters and our borrowing base increases, but we have already had significant delays with them. We do have another option with a traditional ABL group, and a commitment already, based on their due diligence of our most recent financials through April.

Also with respect to financing on the confidentially marketed offering that we did in April, we have almost caught up with our inventory needs, but with production schedules that are on average 30 days out from order and more inventory requirements to keep up with increased demand, we still have a good problem to solve. The good news is, the new Marley Cold Brew is in production in the next few weeks, as is more Marley Mate, more Marley Mellow Mood, more Xing, and more Búcha. We also have 33 containers of Coco-Libre on the water right now as we speak, and the new Xing Craft collection – all in committed distribution is also in production.

Currently, we have enough liquidity to meet demand, but we are in growth mode, and will continue to be tight until the new financing facility is in place.

In summary for the quarter, 95% of our shortfall to internal plan was due to lack of inventory from working capital constraints. Notwithstanding those challenges, we still had our highest first quarter in history. Let me repeat that, our highest first quarter in history, led by international that was up more than 300%. The brands, especially our newest ones, Coco-libre Sparkling, Marley Mate, and Búcha Live Kombucha are selling extremely well and growing – and this is why we remain confident in our guidance for the year, albeit at the low end of the range given our Q1 liquidity constraints.

We do not have the luxury of a big cash balance to fund opportunities, (our company never has). Unfortunately we see tremendous organic growth opportunities right now that we could accelerate – and frankly see some attractive external growth opportunities also. We just are not in a position to address them. Our focus is on continuing to fund the organic growth in the short term, put the new ABL in place, with one party or the other, and just execute the business plan.

And with that, I'd like to pass the call over to Brent.

BRENT WILLIS:

As Chuck mentioned, we still feel confident in outlook for the year at the lower end and continue to hold our team accountable to the plan. The reason for the belief system is all in the revenue. To discuss that, I thought it would be most valuable for our shareholders to hear from the two leaders managing the largest parts of our revenue, Mike Cunningham who leads the US Division, and Josh Hillegass who manages our DSD Division. Let me pass it over to Mike who can give you the facts of what is happening in the market. Mike?

MIKE CUNNINGHAM:

I have been in CPG sales for a very long time, including with world class companies like PepsiCo and Cadbury. Those were great experiences, but I am very excited to be at New Age, especially right now.

I want to address two points. First our brands…and then distribution and how it works. On the brands – we know we have to build our brands or a few key brands with consumers. What's happening, what are the facts? Well on the new brands, Marley Mate, Coco Sparkling, and Búcha we can barely keep them in stock, and the minute we think we're caught up, sales keep growing. It's like what Brent does to us all the time, the minute we think we are caught up, he moves the goal post and asks for more. It's the same way here, trying to keep up with growth.

Where the Brands are in distribution, Búcha is leading its category in sales growth, Marley Mate is leading its category in sales growth, and Coco-Libre Sparkling is actually the first of its kind in its category.

On our core brands …last year in 2017 we integrated them all into one system, one company. I hope everyone understands how much work this actually takes with all our distributors, with all the retailers, with all the systems, and it is incredibly difficult and time consuming. And mind you, we did it while we were transitioning to a lower cost and more effective hybrid route to market, and we did it bringing together 5 different companies. And, on top of that, we have had to reconstruct these brands. We have created new packaging, new formulas, new products, and innovation within the core brands, and frankly, done it at the same time as all the other things. It's a lot of stuff, but at the end result that I see Is increased sales, increased retailer and consumer demand and increased sell through. That's what I see. I see it working.

It would have been great if we would have been able to hold on to all the volume from the core brands in 2017. But that was just not realistic – at all, given when New Age acquired them, they were all declining over a long period of time when they were part of stand-alone, unfunded companies with no resources or capabilities. This is why we were able to acquire them and bring them in to New Age at about a 75% discount to the market average.

Since that time, we've done the hard work, strengthened the brands, gained the distribution, and now, we are growing the core again, and gaining new distribution, in addition to driving new innovations. So I believe the brands are now really getting there. Please don't forget, April is the start of New Age's, first ever sales cycle as a Company. Our first one, and its going great irrespective of the obstacles and growing pains. We have not been a company for more than 10 years like many of our peers. New Age is less than one year old as an integrated Company.

This portfolio strategy is working, and sales per point of distribution is increasing. This one stop shop strategy is unique, and really resonating with both retailers and distributors. It's why we picked up the Military, Dot Foods on the Foodservice side, and a number of new retailers across the country. One of our major natural distributors for example, expects to do more than $12MM with us this year in my division. Last year they did around $1.

That leads me to my second point, distribution. It is a fact, that we have gained right at about 85,000 points of sale. That accomplishment is – well, I don't know any CPG company that has done anywhere near that.

I thought everyone would want to know how distribution works, and when will it show up in the numbers? Here's the process we have to go through. First, we get a retailer to say yes to authorize one of our brands. That cycle that takes almost 12 months. In this industry that is just how it works. Now, please recognize that our new brands and innovation were just finished in Q4 of last year so the fact that we got all this new distribution in Q1 and Q2 means we are actually about 6 months ahead of schedule. Converting the authorization to distribution also takes some time, but here is how it is working in New Age's particular case. Of our 85,000 new points of distribution:

- 20,000 are coming on the Marley family of brands (Mate, Cold Brew, Mellow and Coffee) at a blended 48% gross margin
- 25,000 are coming on the Xing Family, including the new Craft Brew Collection at a blended 35% margin
- 15,000 are coming on Coco-Libre and the new Coco-Libre Sparkling at a blended 52% margin
- 20,000 coming on Búcha Live Kombucha brand at a 43% gross margin
- And 5,000 new points are coming from other brands that are just getting started in traditional and alternative channels at a 59% blended margin

That's the breakdown by brand. Timing wise, we got lucky as most of the distribution was coming in April, May, and June consistent with retailer reset calendars. Had it come in sooner, we would have alienated many of our retail partners. Of the 85 thousand new points, 15,000 were set and in full distribution by end April, another 30,000 will be done by the end of this month (May), and by the end of June the remaining 40,000 points. This equates to, based on our current rate of sales by brand, to monthly revenue of more than $2 million more a month versus our current levels today. We just need the product, the inventory.

So our new challenge is not our brands and sales, it is actually keeping them in stock and keeping the customers happy. In Q1 I had a lot of explaining to do – and I basically told the retailers, that because the brands are growing so well, we are having a tough time keeping up with demand. If they weren't selling, they'd still be on the shelves. It is 100% accurate, and as Chuck mentioned, sort of a good problem to have. Our challenge is we have growing brands, more coming this quarter with Marley Cold Brew, the new Xing Craft Collection, and we have doubled distribution. Our brands with traditional retailers are taking hold we have 3-4 major big box, convenience or grocery channel upsides that we expect to close in the coming quarter, and we are just getting started with Foodservice.

Now I'll turn the call back to Brent.

BRENT WILLIS

Thanks Mike, well done. By the end of the year, we expect our US Division (not including Foodservice) to be more than 40% of our business at a blended margin north of 45%, vs. being less than 30% of the business a little more than 12 months ago.

Josh Hillegass is also joining the call to day. Josh manages what historically is the largest part of our company, our DSD Division. As I have imparted before, this Division is highly strategic for New Age as it provides the business foundation, scale, and resources to enable us to drive our entire business and invest in organic growth. On a standalone basis, Josh's Division delivers positive cash flow and efficient cash conversion, and under his leadership just performs, day in and day out. Josh?

JOSH HILLEGASS

I have had the fortune of leading this Division for the past nine years, and in those past nine years, we have had nine years of consecutive growth. It's all due to a great sales team, merchandising team, driver team, warehousing, shipping, and loading team, and a great team in every other aspect of the business. It has taken years to get this organization and our group in place and I am so proud of them, and the dedication they bring every day to growing New Age and our partner brands. This year will be the 10th consecutive year of growth, and anything else is just not going to happen on our watch.

Similarly to how New Age built the foundation in 2017 in the US Division, we also substantially strengthened our DSD division last year. For more than 10 years, we structured our routes based on experience. Last year we emplaced our first ever routing software, added a number of new routes to increase our distribution universe, and added a number of Hispanic specific routes given the changing demographics in our local market. We strengthened our inventory management and our supply chain processes across the board, and promoted key leaders internally to positions of increasing responsibility. So, we are much stronger as a Division now…than we have ever been before…and are in a position to further scale up.

We felt the same crunch on inventory as Mike did in the US Division. We had a fast start in January and February, on top of an outstanding first quarter in 2017, but felt the impact in March. What sustains us however, and really supports our consistent results is the quality of our brands and brand partners, and the distribution universe we enjoy that encompasses more than 6,000 outlets. We have more than 600 sku's across more than 60 different brand partners with great brands including Nestea, Sparkling Ice, Arrowhead, Jones, Arizona, Essentia Water, Perrier, Bimbo and Takis, Jarritos, New York Seltzer, and too many others to mention.

These are all great brands that are entrusted to us, and together with our own New Age portfolio, we treat our partner brands as our own. We are in the stores every day, increasing presence for them in both depth and breadth, and building these brands at the point of sale where more than 75% of brand choice is made.

We see plenty of growth in front of us in 2018. Driving that is expansion of our routes within existing territory, expanding our distribution reach beyond our current territories, and our new cash and carry business. We are also expanding our channel reach and breadth, to new on-premise outlets and alternative outlets, and within our existing channels and customers, are expanding our depth, with incremental merchandising, displays, and secondary and tertiary points of distribution. All this sounds like basic execution and blocking and tackling – which it is, but we do it well, and that's why we have grown consecutively over the past nine years and will again for an even 10, in 2018. With that, I'll pass it back to Brent.

BRENT WILLIS

Thanks Josh. Both Josh and Mike are outstanding leaders and embodiments of our culture, and there is a direct correlation from their leadership to the superior performance of their Divisions. New Age is lucky to have them and all 169 associates in our Company admire them.

To summarize, we thought it was important to address the inventory challenge in the first four months of the year and its resultant impact. This situation was extremely frustrating not just because of the major institutions that made commitments to us and then didn't deliver, but because of the lost opportunity and more profitable growth that we know is in our grasp.

We also thought it was important to share, the facts in the market and what is happening with our brands and sales, from the leaders directly responsible. To reemphasize a point Mike made, this is our first ever sales cycle for New Age as an a Company. Our first one. As both Mike and Josh mentioned – sales and distribution growth are not our problem, and we have some upside. With retailers and distributors, New Age's one stop shop strategy is working. With consumers, our brands and new products are connecting. Perversely – this exacerbates our inventory and short term working capital issue, because our products are selling at increasing rates. Think about it, that is a very interesting situation to be in, and one that not many, if any others that I know of are encountering.

We never envisioned that our path to achievement of our objectives, was going to be linear. We believe all good things come to those – who absolutely never take no for an answer, and do whatever they have to do to achieve success. That's what we have at New Age and that's why we are here.

And with that I'd like to open it up to questions.