FAMILY INVOLVEMENT

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The purpose of this paper is to share IBG's view of the new emotional and economic realities facing distributors and suppliers in today's fast changing world of consolidation. We have a unique insight into the current environment because we have been involved at all levels for several years.We are aware there are many distributors who own and operate family businesses that they are emotionally attached to. Many are debt free and can sustain themselves with little or no profit. However, over time any business that loses profit loses the ability to perform and one would hope this reality would be difficult for families to accept. Another concern is when good distributors lose their well earned equity value because of outside events or a desire to hold on too long. As suppliers and distributors continue to buy/sell/merge with each other, the consolidation puzzle becomes more complex and the stakes get higher. Brand realignment is a moving target and with each transaction the landscape is altered for everyone. Large swings in values are occurring. Any distributor or supplier that thinks they are immune from the effects of the buy/sell/merge phenomenon is naive. IBG has been and continues to be on the leading edge of the valuation, brand realignment and consolidation process. Let's look at the different issues to consider.

Emotional Issues

Loss of Control – Many distributors are shocked to find out how little control they actually have over their portfolio of brands. Think about InBev, Rolling Rock and Monster moving to the A-B Distributors, Molson shifting to Coors Distributors and Steel Reserve/Sparks going to Miller Distributors. In the past it was insignificant volume and gross profit moving from one to another and no one, except those directly involved in transactions, paid much attention. However, these events are now creating drastic shifts in profitability and consequently the ability of distributors losing brands to perform. The old myth that "as long as I do a good job I'll be ok" is shattered. You can do a great job and lose a brand or a bad job and get a brand. You can be a great performer and suddenly lose the financial incentive to continue your effort. For distributors a significant amount of control has been lost and it is not likely to return any time soon. Suppliers may be a major influence with a distributor today and tomorrow insignificant. Never forget that today's winners could be tomorrow's losers. No one is exempt.

Changing Laws -Whether its litigation by Costco, distributors unable to acquire the brands affiliated with their traditional supplier or suppliers unable to get new brands to its distributors the current legal environment is causing anxiety. Laws that restrict credit, quantity discounts and those requiring in-state residencies will be under enormous pressure as so called franchise legislation is challenged from within the industry. Anything that impedes the ability of brands to move from distributor to distributor could be challenged by suppliers or their traditional distributors. IBG does not take a position on these types of activities but we know they are bubbling to the surface and may soon cause friends to be against friends. States like California, New York, Maryland, Washington, Colorado, Indiana, Kentucky and others allow brands to be moved from one distributor to another with relative ease. As a regulated industry we have always had threats of legal changes so our point is awareness, not panic.

Uncertainty - The world for most distributors/suppliers has been historically stable and predictable. Not today. Consider what has occurred in the past 5 years. Over 400 distributors have left the industry. The big 3 suppliers have lost share. Mega distributors are expanding at the fastest pace ever. Just think about the Reyes Family, Goldring/Moffitt, or A-B with its branch's or partnerships. Then there's Wine and Spirits Distributors like Glazer and soft drink bottlers like Honickman, Clark or Clay.

The point is you can no longer depend on contracts because they may be voided by a transaction and state laws can be changed. These new developments may have had a positive effect for you but taken as a whole they create uncertainties, many of which have been caused by suppliers.

A-B	Bought Grolsh, Rolling Rock Partnered with InBev for over 20 years Partnered with Goose Island, Red Hook,Widmer, Harbin and Tiger Partnered with Monster energy drink
SAB	Bought Miller from Philip Morris
SAB/Miller	Bought O.E.800, Mickey's, Hamm's, Olympia Partnered with Fosters Bought Mackinsey River
CBC	Merged with Molson, bought Carlings in Europe
Gambrinus	Lost Modelo to Crown
Pabst	Became a "virtual" brewer and revitalized Pabst brand
Crown	Gets Modelo from Gambrinus in all 50 states for 10 years
St. Pauli's Girl	InBev brand stays with Crown even though A-B gets InBev
Heineken	Gets Femsa from InBev for 3 years ending in 2007

Economic Issues

<u>Profitability</u> – Even with all these changes IBG feels that the goal must be improving profitability and gaining value. IBG is aware that 2006 has been a pretty solid year in terms of profit for most distributors. But, let's not be rocked to sleep by lower fuel cost, less discounting or accelerating trends of high margin brands. The three-tier system must continually strive to eliminate redundant cost in order to better serve our retailers and consumers without compromising profitability. Specifically we believe distributors need to be efficient enough to operate at 15% cost as a percentage of sales with at least $1.10 per case operating profit. Without this level of profit we believe the ability and incentive to offer full DSD activities will be slowly eroded. IBG supports 50/50 price increases and less pressure on distributors to perform out-dated and unproductive services. We support better retail execution, and more brand marketing by distributors.

Consolidation in General - The days of "easy" buy/sell/merge transactions are history. The ability to sell a distributorship as a whole is no longer the norm. Brands in transition are more vulnerable and suppliers are now more aggressive about conditions for approving the transfer of brands. Previously uninterested distributors are now interested and are seeking all exposed or new brands. Distributors are realizing that a previously difficult exit strategy has suddenly become more difficult. In the tedious process of getting supplier approvals the value of brands are often negatively impacted for the seller because of unreasonable demands on the buyer. Basically the more options a distributor has the higher the price, but with suppliers/distributors consolidating the available options are being reduced. Another consolidation trend is that the high share distributors have more desire and ability to get enough gross profit to render the remaining distributors with enough business to compete profitability. The risk for our industry is that the remaining low share distributors are less able to perform historical DSD services. This trend is difficult to balance but can be accomplished in several different ways. For example:

Distributors that are basically non-competitive in beer can do well by getting into the NA and related beverage business. This can include energy drinks, soft drinks, wine, sports drinks or vitamin waters. For years IBG has marveled at low share distributor's ability to prosper through innovation.

One distributor per market will become more prevalent. Here one distributor might own the warehouse and delivery system but operate separate sales forces. It can be extremely efficient and effective but we have some emotional hurdles to overcome. For some distributors/suppliers this unique approach could be a great strategy.

Shared Services is making a comeback. For several years we have advocated distributors sharing in the cost of any service that has no substantial competitive advantage. Draft line cleaning is an example and IBG has been doing this for over 20 distributors for 7 years. Service is improved and cost is the same or less. There are many other services where this works.

Mega Distributor Trend - As the saying goes "size matters". When it comes to suppliers selecting distributors to represent their brands they almost always go with larger distributors. While one might hear complaints about mega distributor's policies and procedures, they are rarely rejected when it comes to consolidation. There is an economic incentive for distributors and suppliers to push for large, efficient, sophisticated operations that have the financial resources to prosper in rapidly evolving markets. In fact, most mega distributors that IBG has been involved with are generating between $1.00 to $1.50 per case operating profit. Most non-consolidated, mid-size consolidated and small high share distributors that were previously thought to be untouchable are becoming more vulnerable to the mega distributor trend.

Big 3 Supplier Brand Acquisitions - One of the concerns that IBG has for the current trend of top 3 supplier acquisitions is the potential for a competitive imbalance to emerge. Prior to 2000, the top 3 suppliers sold only their traditional brands and distributors could compete with each other in most markets. With its recent acquisitions as well as their investment in Modelo, Anheuser-Busch now has well over 60% of the gross profit under their umbrella. Add a willingness of their distributors to now aggressively seek non aligned SPIM brands and the remaining distributors that are losing these brands may be headed for some tough decisions.

All Other Supplier Consolidation - IBG feels the trend of SPIM suppliers getting together in some capacity will accelerate. We don't know how the teaming up will go but you could see New Belgium/Sam Adams, Yuengling/Sierra, Gambrinus/Mikes, SAB Miller/Boulevard, Molson Coors/Heinekin/Femsa or any combination imaginable. (These are examples not predictions.) This will continue because it is a more efficient way for them to grow their business. While most SPIM suppliers are good operators in their backyard they need size, experience, and higher skill levels to succeed as they expand to new areas. It is easier to partner with someone who has these characteristics than to develop them over time using expensive trial and error methods. Sharing production, administration and freight will also help them get the operational efficiencies necessary for success. The way these suppliers hook-up will have a huge impact on distributors because they will want their brands together in one house. In some regions this could have a deadly or life saving impact depending on who gets what.

Conclusion

The consolidation of brands at the supplier level and the fast development of mega distributors has made realignment more prevalent and more difficult at the same time. Consolidating suppliers need to get their newly acquired brands into one distributor in order to maximize the economic benefits they paid for. Distributors need enough volume and margin to maintain the profitability necessary to continue to deliver high quality DSD services to suppliers/retailers/consumers. Unique issues at the distributor/supplier levels are intensifying with each transaction and retailers/consumers have less tolerance for our unwillingness to adjust to new realities. The rule of thumb seems to be get bigger or get out. Now more than ever you need to be a buyer or a seller. In most cases status quo is an expensive strategy. To approach tomorrow like yesterday will be very costly at the emotional and economic level. This applies to suppliers and distributors. No one is 100% successful but IBG's record and reputation can be verified. We know how to put the parts together, adjust to changes, and emerge with maximum value and working situations for everyone. We keep the process moving and we finish what we start.

Please feel free to contact any of us at any time.