Anheuser-Busch, Inc.

In 1993, Anheuser-Busch (A-B) controlled 46 percent of the U.S. beer market and had clearly established itself as the ruler in the industry. The self-proclaimed "King of Beers" had successfully fought off a challenge by Miller, the second-largest brewer in the industry, to take over the throne. Several of the other top 10 companies in the industry were in trouble and seeking merger partners. They, therefore, presented no threat to the firmly placed crown of A-B, and A-B began seeking to capitalize on its competitors' turmoil.

August Busch III, chairman of A-B, felt very smug about his company's strong leadership position within the industry. He was confident that the company could "continue to dominate its rivals simply by redoubling its efforts—building huge and efficient breweries, spending heavily on advertising and promotion, maintaining price leadership where it holds commanding share, and cutting prices where needed to gain business." According to Dennis Long, president of A-B's Beer Division, "If you segment this country geographically, demographically, and by competitors, it gives you great confidence that there is still considerable room for us to grow."

A-B intended to increase its market share to 55 percent by the year 2000. It was seeking to increase its capacity 27 percent by means of a five-year capital expansion plan. This involved an investment of approximately $2 billion. A previous five-year expansion program costing $1.8 billion increased the capacity of A-B by 50 percent. The major question facing A-B and its chairman was whether A-B would be able to achieve its objectives of increased market share and capacity in light of the decrease in beer consumption growth from five percent annually in the 1970s to less than three percent in 1992. This decrease was a direct result of the increased popularity of other beverages and a decrease in the number of 18- to 34-year-olds.

INDUSTRY BACKGROUND

Small-scale brewing in the United States began in 1633, when the first commercial brewery was founded in the Dutch colonial town of New Amsterdam, now New York City. It was not until the 1840s that large-scale brewing began to take place as a result of the introduction of a different type of yeast from Germany. The 1870s saw the continued evolution of the beer industry when Louis Pasteur developed the process for controlling fermentation. This made the bottling of beer commercially feasible. During the 1900s, two events had a serious impact on the industry. These events were the results of regulatory and technological changes. The first, Prohibition, occurred in 1920, at a time when the industry consisted almost exclusively of local and regional brewers, numbering approximately 1,500 brewers. When Prohibition was repealed in 1933, fewer than 800 of these brewers had survived. The second event, the introduction of commercial television, occurred in 1946. National advertising began to play an important role in determining market leadership. Television gave a definite edge to those brewers who could afford to advertise by placing their brand first in the consumer's mind.

Consolidation of the Industry

Over the past decade, the $10.5 billion beer industry had undergone considerable change. Consolidation occurred as a result of the absorption by large brewers of many regional brewers. There were 92 breweries in 1970, and in 1992 that number

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This case was prepared as a basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

had decreased to 18. In 1992, 79 percent of all the beer sold came from only three of these brewers, and 69 percent was accounted for by A-B and Miller. (See **Exhibit 1**.)

This market dominance by A-B and Miller drastically altered the industry. A-B and Miller paid their unionized employees more than the average wage in the industry, took advantage of economies of scale, and spent more than their competitors for advertising. They gained considerable control over the market as a result of their marketing expertise, an avalanche of money, and a great deal of animosity toward each other. The remaining brewers (except perhaps Coors) provided little challenge for the two leaders. The smaller brewers were suffering from such nightmares as ineffective production and pricing decisions, poor marketing, and continuous management turnover. As a result of their weak position, the smaller brewers banded together. It had been necessary for several of them to merge in order to survive. The long-run outlook for the industry was even greater consolidation.

It appeared that the beer industry was headed toward a controlled oligopoly, similar to that of the tobacco industry. Companies were dissuaded from entering the industry because of high entry costs and low-growth prospects. High entry costs involved two separate considerations: (a) the expense required to build marketing and production groups able to compete with A-B and Miller and (b) the expense and difficulty involved in competing, based on product differentiation. Product differentiation was necessary since price competition alone was not sufficient. However, small brewers were resorting to price cutting in an effort to simply maintain current market shares. This made the low-growth prospects of the industry very apparent. The only small brewer that could possibly compete with A-B and Miller was G. Heileman, because of its low-cost production facilities.

With a reduction in the number of brewers over the long run, it was expected that the number of brands would also decrease. However, this could be offset by new types of beer being offered to new market segments. If greater industry consolidation and stronger competition were to occur in the future, A-B and Miller could potentially benefit from it. A more stable industry would result in an end to the vicious price cutting of the past, and profits would be more easily achieved for the few firms remaining in the industry.

EXHIBIT 1
Market Share in the Beer Industry

Company	*Share in 1981*	*Share in 1992*
Anheuser-Busch	30.3 %	46.2 %
Miller	22.4	22.4
Heileman	7.8	5.3
Coors	7.4	10.4
Stroh	5.0	7.6
Genesee	2.0	1.2
Other	4.7	6.9
Total	100.0 %	100.0 %

Market Shifts

The existing brewers sold different types of beer in all segments of the market. In order to continue expansion, new types of beer were continually produced. The most recent opportunity for growth had come from the light segment. In the 1970s, only three percent of the total market was attributed to light beer. By 1992, light beer accounted for almost one-fourth of the total market. Three factors contributed to the growth in this segment. First, the 25- to 34-year old age group drank the greatest amount of diet soft drinks, and their health-conscious attitudes had an effect on their beer-drinking habits. Although the total population was growing at a rate of one percent annually, this age segment was forecast to grow at a two percent annual rate over the next five years. The second factor involved the increased importance of women in the light beer market. As a group, women appeared to prefer light beer. The third factor contributing to the growth of the light beer segment was advertising. In 1992, Miller held 40 percent of the light beer market; it

had achieved its market leadership by appealing to the more weight-conscious drinker, such as the older male beer drinker.

Imports were another area in which the possibility for growth existed. In 1992, imported beer represented only 4.3 percent of total beer consumption. This market segment was expected to increase by 50 percent in size by the year 2000. Competition in this area is a matter of taste and image. The leading imports were marketed by companies that were not involved with domestic beer products, but most of the larger domestic brewers sold at least one import. Major brewers obviously considered it important to be represented in all segments and regions of the beer market. (See **Exhibit 2**.)

Market Segmentation

To be successful in the national market, three types of strengths were required: marketing skill, product mix, and distribution. The current leaders in the national beer market, A-B and Miller, were strong in all three areas. (See **Exhibit 3**.) They possessed marketing expertise, powerful wholesaler networks, and broad product lines. The strength of their product lines was their focus on the high-margin and high-growth light, premium, and super-premium beer segments. In 1992, A-B and Miller held 68.6 percent of the market, and it was projected that by the end of the decade they would hold 80 percent. Consolidation had accelerated because many small competitors were unable to execute effective marketing programs. It was obvious from this that marketing prowess was necessary for success. Product mix was important because the value of the product mix must be greater than the summed values of the individual products, otherwise referred to as *synergy*. If this is not the case, it would be cost prohibitive to introduce a brand. Effective distribution was also a necessary ingredient to success. There was a tendency among consumers to purchase the brand sold in their neighborhood tavern. In order to capture these on-premise sales, effective distribution was essential. Although distribution strength varied from segment to segment, A-B was strongest in distribution overall.

As mentioned before, imported beer represented a mere 4.3 percent of the market in 1992. This market segment had grown slowly over the preceding five years but was expected to grow to five percent by 1995. Importers continued to expand their markets by introducing new types of beers to appeal to different segments of the drinking-age population (e.g., Amstel Light). Heineken controlled 30 percent of the imported beer market and Molson controlled 20 percent, but recently these brewers had been losing part of their market share to Beck, Moosehead, and Labatt. The major U.S. producers had only recently begun to market one or more types of imported beers. Imported beers had a distinctive taste and were marketed to appeal to consumers who were inner-directed, upscale, and urban. The imported segment was the sole segment

EXHIBIT 2
Principal Brands of Major Brewers

Company	*Premium*	*Super*	*Light*	*Imported*
Anheuser-Busch	Budweiser	Michelob	Budweiser Light	Carlesberg
Miller	Miller High Life	Lowenbrau	Lite	Molson
Stroh	Stroh	Signature	Stroh Light	–
S&P Industries	Pabst Blue Ribbon	–	Pabst Lite	–
Coors	Coors	George Killian's Special Ale	Coors Light	–
Heileman	Old Style	Special Export	Several entries	Beck's

EXHIBIT 3
Strengths of Major Competitors in the Beer Industry in Three Key Areas

Company	*Distribution*	*Marketing Strength*	*Product Mix*
Anheuser-Busch	• Strongest in the industry. • Excellent unit volume increases.	• Superior—after the expenditure of considerable money, time, and effort. • Benefits to both unit volume and productivity.	• The best in the industry. • Something for everyone, but unit volume predominantly in the most profitable segment. • A plus for productivity.
Miller (Philip Morris)	• Far superior to the industry average. • Promotes good unit volume growth.	• Deepest pockets in the industry. • Proven skill. • Benefits to both unit volume and productivity.	• Limited but concentrated in the most profitable segment. • A plus for productivity.
Heileman	• Very strong in some areas and weak in most others. • Unit growth at industry average or slightly better.	• Limited financial strength but very efficient with the dollars it spends. • Makes it a viable competitor in the industry.	• Limited in the most profitable; very strong in the least profitable. • No impact on productivity.
Coors	• Deteriorating in traditional markets; weak in new markets. • Continuing declines in unit volume.	• Thus far, underwhelming. • Both unit volume and productivity declining.	• Limited but concentrated in the most profitable segments. • A potential but unrealizable plus for productivity.
S&P Industries	• Weak and getting weaker. • Continuing declines in unit volume.	• Ineffective and low budget. • Effecting declines in both unit volume and productivity.	• Concentrated in the least profitable segments. • No impact on productivity.

Source: Prudential-Bache's *Brewery Industry Outlook,* March 13, 1993.

of the total beer market that could experience a sales slowdown when the economy decelerated.

The small brewers also marketed beer that had a distinctive taste. These brewers tended to sell on a regional basis, staying in well-defined areas close to home. They specialized in lower-priced beers and controlled less than five percent of the total beer market in 1992. The number of small, local, family-owned breweries had decreased, and it was expected that this trend would continue. Between 1980 and 1990, this market declined substantially in size. As a result of increased fixed costs, many of these brewers had been unable to afford to continue in business on their own. With those that were able to survive, one of the key factors had been community pride and interest in the local brewery.

Competition

There are three areas in which brewers compete with one another: packaging, advertising, and price. Packaging provides brewers with a method of segmentation. Packaging choices include the traditional 12-ounce six-pack in bottles or cans;

20-ounce cans; 40-ounce bottles; 7-ounce eight-pack in bottles or cans; 12-ounce twelve pack in bottles or cans; and various keg sizes. During 1991, 59 percent of the total beer consumed was from cans, 32 percent was from returnable bottles, and nine percent was from nonreturnable bottles. The use of returnable bottles increased significantly since 1991 as a result of the passage of deposit laws in 43 states.

Over the past decade, advertising became the major marketing tool. Since 1987, the advertising expenditures of the major brewers grew by more than 12 percent annually. Effective advertising increased brand loyalties. There was an understanding among brewers to advertise in a legal and morally responsible manner. In order to promote the image of being socially responsible, brewers sponsored many public service commercials involving the subjects of teenage pregnancy and drunk driving. They did not show minors, intoxicated people, or the actual consumption of beer in their advertising. There were several market segments that were important targets of advertising campaigns. These included college students, sports fans, and ethnic groups. The brewers attempted to instill brand loyalty in college students by sending representatives to the campuses (Miller) or by sponsoring activities with promotional samples (Budweiser). The Hispanic market was large and important. To appeal to this market segment, Coors used actors of Hispanic background in its advertising, and A-B used a Spanish advertising agency to promote Michelob.

As new products were introduced, they were targeted directly toward certain market segments. This was achieved mainly through advertising campaigns. Miller Lite was targeted toward older men; Michelob 7-ounce bottles were targeted toward 24- to 35-year-old women. In all the advertisements, focus was placed on identification with males, females, or couples. Beer is an extremely image-oriented product, and advertising campaigns were using a new emphasis. Instead of promoting beer just as a beverage that goes with a simple, relaxed lifestyle, the focus was on beer as a reward for a job well done. In these commercials, beer was the reward after a hard day's work or for winning at a sport. Humor was often injected into the commercials. Advertising played an important role in the beer industry, and it gave those brewers who could afford it a definite competitive advantage.

Price was no longer the important marketing tool it once was. It had lost its competitive importance. The emphasis had shifted to media. Pricing policies now depended upon product positioning. Brewers sold a number of price-sensitive brands, including super-premium, premium, popular-priced, light, and generic beer. It was expected that the premium, super-premium, and light brands would seek annual price increases of six to seven percent compared with the smaller increases of three to five percent sought by the popular-priced brands.

Environmental Factors Affecting the Beer Industry

There were certain economic and demographic factors that affected the beer industry. Two of these factors were the unpredictability of changes in consumer tastes and preferences, and the effect of extended recessionary forces. If the demand for beer was to weaken substantially, this could result in an overcapacity in the industry. Other factors were increased beer consumption by women and the health-conscious attitude regarding lightness and moderation. The potential impact of these factors would be a favoring of beer over distilled spirits that would provide opportunity for enlargement and further segmentation of the beer market. A final factor encompassed all future movements in consumer economics and demographics. One of these forecasted trends was an increase of 20 percent in the 25- to 44-year-old age group by 1997. This age group had a greater amount of discretionary income, tended to eat out more frequently, and was more likely to entertain at home. Another forecasted trend involved the primary beer drinking age segment. The 18- to 24-year-old age group was expected to decrease in size. These projected trends would not be beneficial to the beer industry.

There were also regulatory factors that affected the beer industry. These included stricter litter control requirements, additional legislation requiring bottle deposits, the rise in the drinking age, and increases in the excise tax. If brewers were required to make alterations in their packaging and methods of distribution, the possible result would be increased costs and, therefore, lower profit margins. This also might result if additional legislation were passed requiring bottle deposits. Raising the drinking age would result in shrinking the number of 18- to 24-year-olds who could legally drink, which would also negatively affect brewers' profits. If there was a flat increase in the excise tax, this could lead to a redistribution of profits. The hardest hit by the increase, on a percentage basis, would be popular-priced and generic beers. This could lead consumers to believe that the price differential among brands was narrowing and, therefore, cause them to change to more expensive beers. This might prove devastating to the small regional brewers who specialized in lower-priced beers. Granting permission for territorial agreements between wholesalers would also affect the beer industry. The provision of exclusive regional rights would widen the gap between the strong and the weak wholesalers.

Industry Financial and Operating Performance

In the past, the financial success of brewers paralleled their performance in marketing, distribution, and product mix. The brewers who displayed strength in these three areas gained increasing control over the beer market, whereas the weaker performers had been losing market share.

Even though the gap between the strong and weak brewers had been widening, most brewers' profit margins had been hurt by the price wars of the past. This had somewhat limited flexibility in pricing. As a result, several other components of profitability had become important. These were productivity, unit volume, and gross margin. Productivity could be increased through changes to more favorable product mixes. There had been a shift to brands that had growth opportunities and/or appealing gross profit margins. The gross profit margin of each beer segment and its three- to five-year growth within each segment are shown in **Exhibit 4**.

Both A-B and Miller had focused their product lines on the fast-growing and high-margin light, premium, and super-premium market segments. Light beer was a good brand to market since it was usually less costly to produce, sold at a premium, had a high profit margin, and was, therefore, more profitable than other brands. In 1992, another factor of productivity, operating rate, did not look good for most of the producers in the industry. The average operating rate for the industry was 75 percent of capacity, far below the optimum rate of 90 to 95 percent. A-B was the only brewer with strength in this area; its plants were operating at approximately 98 percent of capacity.

The second important component of profitability was unit volume; the higher the unit volume, the greater the profitability. Since a flattening of beer consumption trends was forecast, the ability of individual brewers to increase their unit volume would depend upon several factors. These included their capacity to finance strong marketing programs and the presence of strong distribution systems.

The third component of profitability was gross margin, which is equal to sales minus cost of goods sold. This figure represented the maximum amount that could be spent on marketing and administrative expenditures without incurring an operating loss. Past and projected industry gross profit is shown in **Exhibit 5**. The industry gross profit per barrel, excluding A-B and Miller, equaled only two-thirds that of A-B. It was not within the financial means of most brewers to reach a competitive level of marketing, since this would necessitate a substantial increase in spending. There was apparently a dichotomy in the industry that could be expressed as "The rich get richer and the not-so-rich are lucky to keep running in place." In summation, higher gross

EXHIBIT 4
Gross Margins in Different Beer Segments

Beer Segment	*Gross Margin For Brewer*	*Gross Margin For Wholesaler*	*% of Industry Volume*
Popular-priced	10% – 16%	20% – 22%	22%
Premium-priced	28% – 30%	25% – 27%	40%
Light beer	30% – 32%	25% – 27%	28%
Super premium-priced	37% – 39%	25% – 27%	2%

Sources: Beverage Industry, Prudential Securities estimates, March 13, 1993.

margins represented more available funds for marketing expenditures. This in turn, led to increased market share and sales, the results of which were greater volume and productivity, and, therefore, increased profitability.

The factors that would affect the future performance of the industry were a slow-growth environment, recession, and the cost outlook. The first factor, a slow-growth environment, would necessitate that even more emphasis be placed on increasing productivity and unit volume. Recession, the second factor, would have an impact upon certain brands of beer, the brands marketed to the people most affected by a recession. A good example of this is Miller High Life, which is strongly marketed toward blue-collar workers. Lastly, the outlook for costs was that (a) the costs of raw materials and packaging would increase at a rate lower than that of inflation and that (b) advertising would not exceed an annual growth rate of 12 percent. Such a favorable cost outlook would enable brewers to keep operating margins within a three to five percent increase. **Exhibit 6** presents a breakdown of the costs of the major brewers.

EXHIBIT 5
Past and Estimated Future Changes in Industry Gross Profit (Profit and Barrelage in Millions)

	1972	*1977*	*1982*	*1992*
Industry				
Total barrelage	131.8	156.9	180.0	209.0
Total gross profit	$1,479.5	$1,915.5	$2,454.5	$3,224.2
Gross profit/barrel	$11.23	$12.21	$13.64	$15.43
Anheuser-Busch				
Total barrelage	26.5	36.6	59.1	86.6
Total gross profit	$392.6	$571.1	$976.1	$1,555.7
Gross profit/barrel	$14.82	$15.60	$16.52	$17.96
Miller				
Total barrelage	5.3	24.2	39.3	54.5
Total gross profit	$71.6	$368.2	$580.7	$865.7
Gross profit/barrel	$13.51	$15.21	$14.78	$15.88
Industry Less Bud and Miller				
Total barrelage	100.0	96.1	81.6	67.9
Total gross profit	$1,015.3	$976.2	$897.7	$802.8
Gross profit/barrel	$10.15	$10.96	$11.00	$11.82

Source: Prudential-Bache's *Brewery Industry Outlook,* March 13, 1993.

EXHIBIT 6
Estimated Cost Breakdown for Major Brewers

Packaging	45 %
Raw materials	15
Labor	12
Marketing	20
All other	8
Total	100 %

Source: Prudential-Bache's *Brewery Industry Outlook,* March 13, 1993.

ANHEUSER-BUSCH PERSPECTIVES

Company Background

A-B was founded in 1852. Its corporate headquarters are in St. Louis, Missouri. The present chairman is August Busch III, a fourth-generation brewer. In 1957, A-B took the industry leadership away from Schlitz and has held this leadership position ever since. During that period, A-B has had to fend off challenges from both Schlitz and Miller. By the 1970s, A-B had grown so contented that even a challenge by Schlitz did not elicit any response. The brewer was running out of beer every summer and saw no need to market aggressively. The challenge by Schlitz failed only as a result of several marketing blunders that cost Schlitz many loyal customers. It was a challenge by Miller, acquired in 1969–70 by Philip Morris, Inc., that posed a definite threat to the leadership position of A-B and prompted it to act. A-B was in the middle of an awkward transition of management when Miller attacked, but what made matters considerably worse was a strike the summer of 1976 that kept its beer off the shelves that summer. In retaliation, A-B made an all-out effort to defeat Miller and successfully retained its leadership position. The war between A-B and Miller badly crippled the rest of the brewers in the industry, who were constantly struggling to survive.

Since 1976, A-B has increased its number of brands from three to 15 to target all market segments. Busch and Natural Pilsner are marketed as popular-priced brands, Budweiser and Budweiser Light as premium brands, and Michelob, Michelob Light, Michelob Classic Dark, and an import as super-premium brands. All of its brands are backed by heavy advertising and promotion expenditures. The amount spent by A-B on media rose 180 percent, to $643 million, between 1981 and 1990. A-B was outspending all other brewers in the sponsoring of sporting events. In 1992, it sponsored 98 professional and 310 college sports events.

Brewers have used "image" advertising to position their products since advertising was first employed, but its use has been on the rise in the past few years. The original targeted beer segment of Budweiser had a strong, rugged image and, therefore, from the beginning, Budweiser had been associated with the Clydesdale horses. A team of these horses pulled the original Budweiser wagon, but their use had become primarily ceremonial. The type of people now drinking Budweiser were higher-income, middle-aged individuals, more likely to be men and less likely to be minorities. In order to attract a broader market, including women, minorities, and older and younger people, A-B established a new campaign to promote Budweiser based on the slogan "This Bud's for you." The overall consumption of Budweiser tended to be evenly distributed geographically. As a result, it did not face the same problem as Miller High Life, which tended to be skewed geographically toward the economically depressed areas of the country. **Exhibit 7** presents the estimated media costs of major competitors.

A-B marketed three light beers, Budweiser Light, Michelob Light, and Natural Light. These three brands were marketed toward the premium, super-premium, and mid-price market segments, respectively. When Budweiser Light was introduced in 1982, it met with unexpected success. This brand emphasized sports and was marketed with a sport-oriented theme, "Bring out your best. . . ." Budweiser Light was targeted toward the heavy beer drinker who was athletic and active, whereas

EXHIBIT 7

Comparison of Advertising Expenditures in the Beer Industry

Advertising Expenditures	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*	*1989*	*1990*
Total Beer Industry	$351.8	$406.5	$494.7	$575.8	$602.5	$688.8	$684.5	$720.4	$677.2	$643.2
% Change		–15.5%	21.5%	16.4%	4.6%	14.3%	–0.6%	5.2%	–6.0%	–3.5%
Anheuser-Busch	$117.2	$164.3	$197.8	$245.8	$270.0	$337.4	$339.0	$369.7	$346.0	$301.1
% Change		40.1%	20.4%	24.3%	9.8%	25.0%	0.5%	9.1%	–6.4%	–13.0%
% of Total Industry	33.3%	40.4%	40.0%	42.7%	44.8%	49.0%	49.5%	51.3%	51.1%	46.1%
Market Share	30.0%	32.4%	32.9%	35.0%	37.1%	38.6%	40.6%	41.9%	43.0%	44.6%
Miller	$91.1	$115.5	$133.9	$163.7	$163.5	$201.2	$170.9	$168.4	$149.5	$188.6
% Change		26.8%	15.9%	22.3%	–0.1%	23.1%	–15.1%	–1.5%	–11.2%	26.2%
% of Total Industry	25.9%	28.4%	27.1%	28.4%	27.1%	29.2%	25.0%	23.4%	22.1%	28.9%
Market Share	22.2%	21.5%	20.4%	20.5%	20.2%	20.5%	20.8%	21.5%	22.2%	22.7%
Coors	$23.0	$22.1	$30.4	$38.1	$58.4	$77.7	$84.7	$111.1	$114.3	$122.4
% Change		–3.5%	37.3%	25.2%	53.3%	33.2%	9.0%	31.2%	2.9%	7.1%
% of Total Industry	6.5%	5.4%	6.1%	6.6%	9.7%	11.3%	12.4%	15.4%	16.9%	18.7%
Market Share	7.3%	6.5%	7.5%	7.2%	8.0%	8.1%	8.4%	8.8%	9.5%	9.9%

Source: Beverage Industry and Leading National Advertisers.

Miller Lite was targeted toward the older male beer drinker who was weight conscious.

Busch, a popular-priced beer, was targeted toward the free-spirited man. Promotional campaigns for this brand were geared toward the hard-working blue-collar employee who headed to the mountains for relaxation. The super-premium market segment was dominated by Michelob, an A-B brand, and close behind was Lowenbrau, a Miller brand. There had been a slowing in the growth of this market segment. The new promotional campaign for Michelob Light targeted white-collar men and women who entertained, belonged to country clubs, and could afford to spend a little more for a special occasion beer. This campaign centered on heritage, tradition, quality, and distinctiveness. A-B, with its many expenditures on advertising, closely followed by Miller, was the leader of the industry.

Wholesalers have high fixed expenses as a result of the large capital outlays required to purchase trucks, etc. Therefore, a wholesaler depends on volume sales for profit and concentrates effort upon the brands that offer the greatest volume. It can be seen in **Exhibit 8** that A-B and Miller had greater volume than competing brewers. A-B achieved product distribution through a network of 950 wholesalers and was reputed to have the most effective network of wholesalers in the industry. A-B had provided considerable support to its wholesalers, including the establishment of in-depth training seminars on financial management and warehousing. Wholesaler performance was evaluated on the basis of the frequency with which calls were made upon accounts, the weekly and monthly sales of all beers, and several other factors. It was normal for an A-B wholesaler to hold from 12 to more than 20 days' inventory, depending on the season. With a high inventory turnover rate, a wholesaler was able to generate profits much more quickly. The effective wholesaler system of A-B proved invaluable since it was forecast that, in the future, the fight between the brewers would be focused at the wholesaler level.

EXHIBIT 8
Average Case Volume per Brand per Distributor for Different Brewers

AnheuserBusch	859,000
Miller	637,000
Heileman	108,000
Coors	438,000
Stroh	280,000
S&P Industries	154,000
Industry average	541,000
Industry average less A-B	405,000

Source: Prudential-Bache's *Brewery Industry Outlook,* March 13, 1993.

Company Financial and Operating Performance

A-B's many interests include baking operations, snack foods, transportation services, a baseball franchise, and real estate development. Despite these other interests, A-B's beer operations dominate its revenue base. The beer operations accounted for approximately 85 percent of revenue in 1992. As of June 1992, A-B controlled 46 percent of the U.S. beer market. It controlled 31.4 percent in 1982, 28.2 percent in 1980, and 23 percent in 1977. This was an increase in market share of 44 percent between 1982 and 1992. The volume of beer sold by A-B also increased significantly over these ten years. In 1982, A-B had total sales of $5.3 billion, and its profit for the year was $287.3 million. In 1992, A-B's sales amounted to more than $13 billion, while the net income was $917 million. **Exhibit 9** presents the financial and operating performance of A-B.

Over this ten-year period, A-B experienced an increase in sales and profits of 150 percent and 220 percent, respectively. (See **Exhibit 10**.) It had a unit profitability of approximately $3.59 per barrel of beer sold, greater than that of the rest of the industry. Although it was forecast that total market earnings would increase by 15 to 20 percent in 1993, it was projected that A-B earnings would increase by 30 to 40 percent. As a result of its profit leadership in the industry, A-B had price elasticity.

EXHIBIT 9
Consolidated Balance Sheet—Anheuser-Busch Companies, Inc., and Subsidiaries

Assets (In millions) *December 31,*	*1992*	*1991*
Current Assets:		
Cash and marketable securities	$ 215.0	$ 97.3
Accounts and notes receivable, less allowance for doubtful accounts of $4.9 in 1992 and $5.5 in 1991	649.8	654.8
Inventories—		
Raw materials and supplies	417.7	397.2
Work in process	88.7	92.5
Finished goods	154.3	145.9
Total inventories	660.7	635.6
Other current assets	290.3	240.0
Total current assets	1,815.8	1,627.7
Investments and Other Assets:		
Investments in and advances to affiliated companies	171.6	116.9
Investment properties	164.8	159.9
Deferred charges and other non-current assets	356.3	365.6
Excess of cost over net assets of acquired businesses, net	505.7	519.9
	1,198.4	1,162.3
Plant and Equipment:		
Land	273.3	308.9
Buildings	3,295.2	3,027.8
Machinery and equipment	7,086.9	6,583.9
Construction in progress	729.7	669.0
	11,385.1	10,589.6
Accumulated depreciation	(3,861.4)	(3,393.1)
	7,523.7	7,196.5
	$10,537.9	$ 9,986.5

A-B experienced operating and financial success as a result of both productivity gains and unit volume increases. It spent more than $2 billion over the past five years on a program to increase capacity. This both expanded and upgraded the cost-effectiveness of the A-B plants. Over the next five years, A-B intended to invest another $2 billion in order to increase capacity from 62 million barrels to over 75 million. A significant portion of these funds was likely to be internally generated. A-B acquired the second-largest domestic baker, Campbell-Taggert, which should result in an increase in the amount of funds generated internally.

A-B successfully positioned its products in the high-margin and fast-growing beer segments. It also employed an aggressive marketing strategy. As a result, A-B achieved increases in unit volume that were greater than the growth in industry sales. Over the next five years, it was projected that annual unit growth for A-B would be 8 to 10 percent. In order to obtain operating flexibility, A-B

EXHIBIT 9 ***(continued)***
Consolidated Statement of Income—Anheuser-Busch Companies, Inc., and Subsidiaries

(In millions, except per share data) *Year Ended December 31,*	*1992*	*1991*	*1990*
Sales	$13,062.3	$12,634.2	$11,611.7
Less federal and state excise taxes	1,668.6	1,637.9	868.1
Net sales	11,393.7	10,996.3	10,743.6
Cost of products and services	7,309.1	7,148.7	7,093.5
Gross profit	4,084.6	3,847.6	3,650.1
Marketing, distribution and administrative expenses	2,308.9	2,126.1	2,051.1
Operating income	1,775.7	1,721.5	1,599.0
Other income and expenses:			
Interest expense	(199.6)	(238.5)	(283.0)
Interest capitalized	47.7	46.5	54.6
Interest income	7.1	9.2	7.0
Other income/(expense), net	(15.7)	(18.1)	(25.5)
Income before income taxes	1,615.2	1,520.6	1,352.1
Provision for income taxes:			
Current	561.9	479.1	429.9
Deferred	59.1	101.7	79.8
	621.0	580.8	509.7
Net income, before cumulative effect of accounting changes	994.2	939.8	842.4
Cumulative effect of changes in the method of accounting for postretirement benefits (FAS 106) and income taxes (FAS 109), net of tax benefit of $186.4 million	(76.7)	–	–
Net Income	$ 917.5	$ 939.8	$ 842.4
Primary Earnings per Share:			
Net income, before cumulative effect	$ 3.48	$ 3.26	$ 2.96
Cumulative effect of accounting changes	(.26)	–	–
Net income	$ 3.22	$ 3.26	$ 2.96
Fully Diluted Earnings per Share:			
Net income, before cumulative effect	$ 3.46	$ 3.25	$ 2.95
Cumulative effect of accounting changes	(.26)	–	–
Net income	$ 3.20	$ 3.25	$ 2.95

Note: During 1992 the company elected to early adopt the new Financial Accounting Standards pertaining to Postretirement Benefits (FAS 106) and Income Taxes (FAS 109). This decision affects the comparability of 1992 reported results with those of prior years. Management believes that readers of the company's financial statements need to be fully aware of the impact the adoption of these Standards has on 1992 operating results and earnings per share. Excluding the financial impact of these Standards, 1992 operating income, income before income taxes, net income and fully diluted earnings per share would have been $1,830.8 million, $1,676.0 million, $1,029.2 million and $3.58, respectively.

EXHIBIT 10
Financial Summary–Operations, Anheuser-Busch Companies, Inc., and Subsidiaries

(In millions, except per share data)	*1992*	*1991*	*1990*
Consolidated Summary of Operations			
Barrels sold	86.8	86.0	86.5
Sales	$13,062.3	$12,634.2	$11,611.7
Federal and state excise taxes	1,668.6	1,637.9	868.1
Net sales	11,393.7	10,996.3	10,743.6
Cost of products and services	7,309.1	7,148.7	7,093.5
Gross profit	4,084.6	3,847.6	3,650.1
Marketing, distribution and administrative expenses	2,308.9	2,126.1	2,051.1
Operating income	1,775.7(1)	1,721.5	1,599.0
Interest expense	(199.6)	(238.5)	(283.0)
Interest capitalized	47.7	46.5	54.6
Interest income	7.1	9.2	7.0
Other income/(expense), net	(15.7)	(18.1)	(25.5)
Gain on sale of Lafayette plant	–	–	–
Income before income taxes	1,615.2(1)	1,520.6	1,352.1
Income taxes	621.0	580.8	509.7
Net income, before cumulative effect of accounting changes	994.2(1)	939.8	842.4
Cumulative effect of changes in the method of accounting for postretirement benefits (FAS 106) and income taxes (FAS 109), net of tax benefit of $186.4 million	(76.7)	–	–
Net Income	$ 917.5	$ 939.8	$ 842.4

Source: Annual Report of the Company.

also employed vertical integration. Many of the processes involved in the manufacturing of beer were carried on in-house at the A-B facilities. These included barley malting, metalized paper printing, and can manufacturing. Although A-B was putting considerable effort into expansion, other brewers were attempting to increase their return on investment by restricting capacity.

Expansion

In the 1970s, A-B was unsuccessful in its efforts to market root beer and a low-alcohol lemon-lime drink. As a result of these past failures, the company was moving into new areas more cautiously. Also, A-B teamed up with partners for certain ventures. It moved into the rapidly expanding "wine on tap" business with a partner, LaMont Winery, Inc. In this business, A-B was marketing larger kegs that distributed white, red, and rosé wines under the Master Cellars brand name. A-B also expanded through diversification into the snack food business. Its Eagle Snacks were being distributed nationwide through bars and convenience stores. The company's latest offering in the beer market was O'Doul's, a non-alcoholic beer. It was hoped that this brand would succeed well in the new, emerging non-alcoholic segment.

In planning the future expansion of A-B, August Busch III had several strategic alternatives to consider. These could be divided into two categories: those involving beer operations and those

EXHIBIT 10
(continued)

1989	1988	1987	1986	1985	1984	1983	1982
80.7	78.5	76.1	72.3	68.0	64.0	60.5	59.1
$10,283.6	$ 9,705.1	$ 9,110.4	$ 8,478.8	$ 7,756.7	$ 7,218.8	$ 6,714.7	$ 5,251.2
802.3	781.0	760.7	724.5	683.0	657.0	624.3	609.1
9,481.3	8,924.1	8,349.7	7,754.3	7,073.7	6,561.8	6,090.4	4,642.1
6,275.8	5,825.5	5,374.3	5,026.5	4,729.8	4,464.6	4,161.0	3,384.3
3,205.5	3,098.6	2,975.4	2,727.8	2,343.9	2,097.2	1,929.4	1,257.8
1,876.8	1,834.5	1,826.8	1,709.8	1,498.2	1,338.5	1,226.4	758.8
1,328.7	1,264.1	1,148.6	1,018.0	845.7	758.7	703.0	499.0
(177.9)	(141.6)	(127.5)	(99.9)	(96.5)	(106.0)	(115.4)	(93.2)
51.5	44.2	40.3	33.2	37.2	46.8	32.9	41.2
12.6	9.8	12.8	9.6	21.3	22.8	12.5	17.0
11.8	(16.4)	(9.9)	(13.6)	(23.3)	(29.6)	(14.8)	(5.8)
–	–	–	–	–	–	–	20.4
1,226.7	1,160.1	1,064.3	947.3(2)	784.4	692.7	618.2	478.6
459.5	444.2	449.6	429.3	340.7	301.2	270.2	191.3
767.2	715.9	614.7	518.0(2)	443.7	391.5	348.0	287.3(3)
–	–	–	–	–	–	–	–
$ 767.2	$ 715.9	$ 614.7	$ 518.0(2)	$ 443.7	$ 391.5	$ 348.0	$ 287.3(3)

involving nonbeer operations. Within the beer operations category, there were several possible alternatives for expansion, including the light beer segment, acquisitions, European markets, divestitures, the Eastern bloc, and the 3.2 beer segment. There was definitely opportunity for expansion through the light beer segment because it was estimated that the potential for market penetration was at least 40 percent and current penetration was only 25 percent. It would also be possible for A-B to expand through the acquisition of smaller brewers. The disadvantage of A-B acquiring smaller brewers would be that most of these brewers tended to concentrate on unique market segments that would be too small or uneconomical for A-B to serve. Therefore, these acquisitions might offer few advantages. However, it might prove necessary to acquire some smaller brewers in order to stop them from banding together and establishing a third power in the industry.

Another way in which A-B could promote expansion was through European markets. It would be beneficial for A-B to explore and evaluate untapped European markets. The question mark in this alternative was whether A-B brands would be able to compete successfully against the heavier, fuller European brands. It could also prove beneficial to A-B to divest its Natural Light brand of beer, which had proved to be unsuccessful. In 1992, this brand was lowered in price when selling to supermarket accounts, since this was where consumers were extremely price sensitive. It appeared that the consumer was not attracted to A-B's idea of a "natural" beer as A-B had expected. There was

potential for further expansion if A-B divested its Natural Light brand and used these brewing facilities for the production of Budweiser Light.

Another possible alternative for A-B was to put a vigorous effort into pursuing "Eastern" markets. It appeared that the Japanese were extremely attracted to products that project "Western" culture. The Japanese company that marketed Suntory whiskey was promoting the product in California to encourage its projection of a "Western" image so that it would be accepted in Japan. An aggressive marketing effort in this area of the world should promote the expansion of A-B. Expansion could also be promoted through pursuit of the 3.2 beer market segment. This variety of beer has half the alcohol, and thus half the calories, of regular beer. The only problem with pursuing this market segment was that it could affect the sales of light beer, which also has fewer calories than regular beer.

The other category of alternatives through which expansion could be achieved involved nonbeer operations. The major questions concerning Eagle Snacks and their potential for expansion involved the growth of the snack food market, how the product could be differentiated, and whether or not the product could obtain a significant part of the retail business, considering Frito-Lay's market domination. A-B could potentially expand through growth in the snack food business.

The other area through which A-B could expand was wine and spirits. **Exhibit 11** compares the 1992 consumption of various liquids, such as beer, wine, spirits, etc. A-B had already moved into the "wine on tap" business with a partner. There were a number of other possibilities in this area it could explore. One of these possibilities involved determining the feasibility of acquiring a winery and taking advantage of A-B's strengths in distribution and marketing. Another possibility involved exploring the potential for developing a product to compete with "Club Cocktails," currently marketed by Heublein, Inc. A-B has great potential for further expansion since its strengths allow it to diversify. It has many possibilities to consider for future expansion.

To sum up, the future outlook for A-B is good. Its facilities were operating at 98 percent of capacity, and the brewer was confident that it could maintain its dominance in the industry. August Busch III was not fazed by slowing beer consumption and was confident that A-B could achieve its objectives of increased market share and capacity. If the company continued its aggressive marketing strategy and capitalized upon its ability to diversify and expand in other areas, there appeared to be no reason why it would not achieve its objectives.

EXHIBIT 11
1992 Liquid Consumption in the U.S. (Gallons per Capita)

Soft drinks	40.1
Coffee	26.1
Beer	24.4
Milk	20.5
Tea	6.3
Powdered drinks	NA
Juices	6.6
Spirits	1.9
Wines	2.3
Bottled water	2.2
Water	46.1
Total	176.5

Source: Beverage Industry, May 14, 1993.