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Market Dynamics

Functional Beverages
Market Dynamics: Summary

The market for functional drinks in the U.S. is valued at $27B

- The market for functional drinks in the U.S. grew by 7.4% in 2013 to reach a value of $27 billion
- Energy and sports drinks accounted for 82% of the total functional category in 2013, but the protein segment experienced the most growth
- In 2013, all five functional beverage sub-segments grew for the first time since
- 2010, although overall growth was only 2.1%
Growth slows, but is still strong at 8.7%

Demand for healthy beverages drives growth of functional drinks segment to $27B

The market for functional drinks in the U.S. grew by 7.4% in 2013 to reach a value of $27 billion. The CAGR for the market in the period 2009–13 was 8.7%.

Source: MarketLine
While protein drinks only accounted for 1.4% share of the functional category last year, the segment is experiencing the strongest growth of any sub-segment.

Protein drinks grew by 7.9% in just one year between 2012 and 2013.
Energy Drinks Show Most Consistent Growth

Over a five-year period, Energy Drinks have shown the most growth in the segment

In 2013, all five functional beverage sub-segments grew for the first time since 2010, although overall growth was only 2.1%.

Source: Beverage Marketing Corporation
Protein Drinks: Small but Strongest Growth

Energy and Sports Drinks accounted for 82% of the total functional category in 2013

- In 2012, Grocery was the leading distribution channel in the United States functional drinks market, accounting for a 72.3% share of the total market's volume.

- On-trade accounts for a further 10.8% of the market.
In 2017, the United States functional drinks market is forecast to have a value of $38.5 billion, an increase of 52.8% since 2012. The CAGR for the period 2012–17 is forecast to be 8.8%.

Source: MarketLine
Category Trends

Functional Beverages
Category Trends: Summary

- The category is being influenced strongly by consumer focus on protein, wellness, natural and “free-from” trends, among others.

- Key consumer segments driving growth of functional beverages include aging consumers searching for vitality, Millennials who are more comfortable trying products with wellness benefits and busy consumers looking for “quick health”.

- Energy drinks as a subcategory continue to grow, though growth is slowing which may suggest maturation. Key trends impacting this subcategory include shots and low/no calorie offerings.

- Sports drinks face increasing competition from other beverage categories offering consumers increasingly comparable functionality.
Cultural focus on protein, wellness, natural and “free from” are all driving innovation in the functional drink space.

Source: Nutraceuticals World, 2014
Category growth driven by those seeking “fast wellness”

- Three key consumer segments drive the search for convenience in functional beverages:
  - Aging population looking to maintain vitality
  - Millennials, who are open and interested in trying food and beverage with wellness benefits
  - Consumers on the go with busy lifestyles, seeking wellness without work

“The trend for health and wellness has never been stronger. Health conscious consumers are seeking a healthier alternative to the more traditional soft drinks on the market. In supermarkets, a new health and wellness category is being established, and filled with beverages that are fortified, healthy, natural and low calorie. The market for functional beverages is on an upward trajectory and this trend is set to continue.”

-- Sarah Battledore, LycoRed

Energy Drink growth driven by flavor, natural ingredients and low/no calorie and sugar claims

- In general, energy drink flavors are becoming more sophisticated. The use of superfruit and berry flavors, in particular, are gaining momentum.

- Consumers seem to be responding positively to these flavor expansions. Monster Beverage Corp.’s coffee-flavored Java Monster energy drink grew nearly 12% in the 52 weeks ending April 20, according to data from IRI.

- Beyond flavor, energy drink brands also are experimenting with natural energy ingredients, such as coconut water and fruit juice, to offer “healthy energy.” For instance, Rockstar launched Rockstar Energy + Hydration Coconut Water Energy Drink, which is a non-carbonated energy drink made with 10% coconut water.

- Within the energy shots segment, ingredients like kombucha and beetroot are being used for functional claims. The Hain Celestial Group, for example, launched a line of kombucha shots under its Celestial Seasonings brand with natural energy ingredients, including raw kombucha, guarana, ginseng and B vitamins to supply energy.

- Sugar-free and calorie-free energy drinks and shots also are a notable trend in the category, according to experts. Monster Energy Zero Ultra, which does not contain calories or sugar, grew 150 percent during the 52 weeks ending April 20 in IRI-measured channels compared with the prior-year period.
Sports Drink category faces competition from Nutritional Drinks

After a strong growth period, the sports drink category is facing competition from brands outside the category. According to Mintel, the sports drink category grew 30% from $5.4 billion to nearly $7 billion between 2008 and 2013. However, it now is facing outside challenges.

The U.S. sports drink market began to slow in 2012 and was essentially flat in 2013. According to IRI, the non-aseptic sports drink category increased just shy of 2%, totaling more than $5.5 billion in sales for the 52 weeks ending April 20 in total U.S. multi-outlets.

Accounting for roughly 99% of the market are PepsiCo and The Coca-Cola Co., PepsiCo’s Gatorade and Propel brands make up 77.7% of the market, while The Coca-Cola Co.’s Powerade brand represents 21.3%, based on IRI data.

The sports drink mix category also has seen major gains from Kraft Foods Inc. The company’s Mio Fit brand saw sales increase nearly 150 percent, totaling $21 million for the 52 weeks ending April 20 in IRI-measured channels.

However, consumers also are turning to other solutions when it comes to their healthy beverage purchases. Smaller than the sports drink category, nutritional drinks, including meal replacement beverages, accounted for less than half of the sales of sports drinks in 2013 at $3.2 billion. Even smaller than that was protein drinks with $2.1 billion in sales for 2013; however, this is a 51.2 percent increase from 2011 when sales were $1.4 billion.

Source: Beverage Industry 2014 State of the Industry
Functional beverages hitting the market at Expo West

Blu-Dot protein teas offer 12 g of protein from whey protein and 6 g fiber per bottle. The teas are sweetened with cane sugar, or are available in reduced-calorie varieties that are sweetened with stevia.

Lifeway Protein Kefir offers 20 g protein per serving, as well as 12 live and active probiotic cultures. Another example is Slingshot yogurt protein drinks with a crunchy shot, which provide at least 18 g protein in addition to probiotics, fiber and omega-3s.

ULIVjava iced coffee beverages by Martha Stewart, are enhanced with herbs and botanicals, including green tea, yerba mate and astragalus. The green tea promotes weight loss, while antioxidants from yerba mate are intended to enhance physical endurance, and astragalus improves vitality via its adaptogenic properties.

EnerBee Organic Energy beverages support the HoneyBee Alliance, a network of individuals, groups and organizations that work to increase awareness and support of the honeybee population. Energizing ingredients include green tea, yerba mate, ginseng, B vitamins and 100 mg organic caffeine.

Whole e Coco complete coconut elixir, by Whole e Nature, is made from all-natural ingredients and offers 9 g of medium-chain triglyceride (MCT) oils, including lauric, caprillic and capric acid, for energy and improved satiety. The beverages are also non-GMO, dairy-free, vegan, gluten-free and kosher.

Yogi launched its Cranberry Spice Probiotic Balance tea, which contains a non-allergenic version of Ganeden’s BC30, as well as cranberry and Hawthorne berry for digestion.

Source: Food Product Design
Key Players

Functional Beverages
PepsiCo was the largest player in functional beverages in 2013. Coca-Cola increased from 17.8% of the market in 2008 to 18.5% in 2013. The biggest gainer has been Monster Beverage Corporation, which has seen its share jump from 6.4% in 2008 to 10.1% in 2013.
Pepsi and Coke own this category, but Monster’s share is growing fastest

PepsiCo was the largest player in functional beverages in 2013. Coca-Cola increased from 17.8% of the market in 2008 to 18.5% in 2013. The biggest gainer has been Monster Beverage Corporation, which has seen its share jump from 6.4% in 2008 to 10.1% in 2013.

Source: Beverage Marketing Corporation
Monster Beverage Company

Competitor Profile

Overview

- Monster Beverage develops, markets, and distributes a wide assortment of beverage products. The company's products include natural sodas, fruit juices and juice drinks, energy drinks and sports drinks, and fruit juice smoothies.

- The company operates through two business segments: direct store delivery (DSD) and warehouse.

Product

Key Financials

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Performance

- Graph showing trends in revenues, net income, and profit margin from 2008 to 2012.
Coca-Cola Competitor Profile

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<tr>
<td>Profit margin</td>
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<td>Liabilities growth</td>
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![Graph showing revenues, net income, and profit margin over years](image)
PepsiCo
Competitor Profile

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<th>2009</th>
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<tr>
<td>Profit margin</td>
<td>11.9%</td>
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<td>9.7%</td>
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<tr>
<td>Revenue growth</td>
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<td>0.0%</td>
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<tr>
<td>Asset growth</td>
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<tr>
<td>Liabilities growth</td>
<td>37.3%</td>
<td>(6.2%)</td>
<td>108.3%</td>
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<td>71.3%</td>
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<tr>
<td>Return on assets</td>
<td>14.6%</td>
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![Graph showing revenues, net income, and profit margin](image)
Red Bull

Competitor Profile

- Red Bull is a manufacturer and marketer of energy drinks. The company produces energy drinks in Austria and exports them to around 165 countries. The company markets its products under the brand name of "Red Bull."

- The company's products include the following: Red Bull Energy Drink, Red Bull Sugarfree, Red Bull Zero Calories and Red Bull Editions.

- Red Bull Energy Drink and Red Bull Sugarfree are functional beverages. Red Bull Zero Calories is a mix of ingredients that contains a range of caffeine, B-group vitamins, taurine, aspartame, sucralose and acesulfame K, and alpine spring water. Red Bull Editions product is offered under three different flavors which include cranberry, lime and blueberry.
Five Forces Analysis

Functional Beverages
The US functional drinks market is concentrated, with the top three players holding 70.8% of the total market share.

In the global functional drinks market food retailers are the main buyers, and may exert strong buyer power, especially if they are large chains. However, they are motivated to stock many functional drinks due to end-user demand.

The main inputs to the market include ingredients such as fruit, milk and herbal extracts.

Manufacturers may be larger companies than suppliers, but most suppliers are not heavily reliant on functional drinks manufacturers for their revenues which increases their strength in the supply chain.

The growth of the market encourages new entrants, although they will need to contend with large incumbents that own strong brands.

Players present in this market are generally large but very diverse companies, which eases rivalry.

Source: MarketLine
Buyer Power

Five Forces Analysis

In the US, supermarkets and hypermarkets are the most significant distribution channel for functional drinks, sharing about 72.3% of the total market, which strengthens the buyer power. Switching costs for retailers are not that high.

However, consumer demand motivates stores to stock functional drinks of some type.

Product differentiation is driving the market and is visible in terms of different flavors and nutritional benefit which again weakens buyer power. At the same time, the trend for "health and wellness" is becoming increasingly popular among consumers who look for new ways to balance their diet. This means that manufacturers must meet the increasing demands of consumers for whom health and well-being is important. To meet the new trend in the functional food market buyers stock the so-called life-style products, which are adapted to the style of life, diminishing buyer power to some extent. The example here may be products for women that support the cultivation of beauty, such as beverages containing aloe vera. However all functional drinks ultimately aim to produce similar effects.

Some of the major retailers such as supermarkets have integrated backwards in the sense that they offer private-label versions of energy drinks. Private label functional drinks proved to be a significant ingredient in the diet of end-users, indicating that the price, even for such specific products for which consumers have high expectations, is an important determinant of the purchase.

Overall buyer power in this market is assessed as moderate.
Supplier Power

Five Forces Analysis

Suppliers in this market include those entities supplying ingredients and equipment for the production of functional drinks.

Ingredients used include fruit, milk, sugar, caffeine, herbal extracts and other ingredients such as taurine, glucuronolactone, guarana, electrolytes, aspartame and vitamins. Farmers are the main suppliers of fresh ingredients such as fruit and milk. The quality of these ingredients is crucial to maintaining confidence in the product. These suppliers are usually small compared to manufacturers and thus supplier power is reduced.

Some essential commodities are available from several sources, although, like every product, they are subject to price fluctuations. Some ingredients (e.g. aspartame) are available from only one or two companies upstream. However, even in these cases, there are usually substitutes available: for example, if aspartame becomes expensive or unobtainable, functional drinks manufacturers could consider using saccharine.

Packaging is another important input in this market and some market players enter into long-term contracts with their suppliers which strengthens supplier power.

Other suppliers include those providing advertising services to market players; a strong brand image is key to securing success in this market.

Overall supplier power is assessed as moderate in this market.

Source: MarketLine
New Entrants

Five Forces Analysis

For several years energy drinks were at the core of the entire functional drink category. The prediction of swift concentration among producers and supplier were supposed to practically eliminate the smallest players. According to present data, however, the functional drinks market is thriving, both in value and volume of sales. There are no indications that this trend will be altered soon. The healthy growth in market revenues during the past few years should encourage new entrants. The increase in sales of functional drinks is mainly due to the modern lifestyle, reduction in the average prices of the products, and the introduction of differentiation in packaging.

Entry to this market can be done either as a small start-up company or as an existing company diversifying into the market. Many soft drinks manufacturers have the capability to penetrate this market successfully, as there would be little requirement to invest in new equipment or adapt the company’s business model. An entirely new company could enter the market on a small scale and operate a single integrated retail outlet, particularly with fresh, fashionable drinks such as smoothies. However, to appeal to the mass-consumer market, a company would need to be reasonably large, in order to obtain scale economies in production. Brand building would also be a requirement if a new company were to succeed in this market.

Good market growth is expected to continue mainly due to improvements in the composition of products and the introduction of increasingly innovative, functional drinks. For example, new segments in the market such as “relaxation drinks” being the opposite of energy drinks.

Overall the likelihood of new entrants is assessed as moderate.

Source: MarketLine
For the consumer, substitutes for functional drinks include a range of products offering similar nutritional content in what are arguably less convenient or less effective forms.

For example, energy drinks face indirect competition from more traditional caffeine-containing drinks such as coffee; conventional soft drinks, confectionery, or fresh fruit are (partial) substitutes for sports drinks, and so on. Retail and on-trade buyers in this market already offer these products to consumers, and from their point of view, the benefits of functional drinks over conventional soft drinks can include higher margins, while the benefits over fresh fruit include longer shelf life and so less costly wastage. Disadvantages might include the need for more costly chilled storage for functional drinks, in order to appeal to the consumer.

Overall, the threat of substitutes is assessed as moderate.

Source: MarketLine
Degree of Rivalry

Five Forces Analysis

The US functional drinks market is concentrated, with the top three players holding 70.8% of the total market value. The diversity of functional beverages includes differences in functional additives, specific time of day drinks (such as breakfast drinks), drinks aimed at various age groups, and special occasions.

Some players in this market, such as Red Bull, are exclusively focused on functional drinks. However, they are facing increasing competition from large scale, diversified drinks manufacturers such as Coca-Cola and pharmaceutical companies such as GlaxoSmithKline. GSK produces the energy drink Lucozade and is highly diversified, reducing its dependence on the functional drinks market.

There are many other products on the buyers shelves. Such a differentiation of products lowers the level of rivalry but at the same time decreases the commodities’ price and forces players to spend more on advertising, thus increasing rivalry.

Exit costs for the functional drinks business overall are dependent on the extent to which production is outsourced. More business functions under the control of the manufacturer lead to higher exit barriers, due to the need to divest its assets such as specialized equipment.

However, simply exiting the functional drinks market, while remaining in the larger soft drinks business, would not be particularly costly, as most of the production process would remain the same, only the ingredients would alter. Fixed costs are fairly high, and it is often necessary to incur costs in research and development, particularly when testing the health benefits of probiotic drinks etc.

Overall rivalry in this market is moderate.

Source: MarketLine