

beverage REPORT

part 2

A CASE OF THE JITTERS

Retailers seek merchandising strategies for hopped-up energy category

By Jerry Soverinsky

It's just past midnight on an unseasonably warm December Chicago night. The hip Lakeview neighborhood, just blocks from Wrigley Field, is alive with activity. I wander into a convenience store, pay for a large coffee and grab a stool by the window to watch a kaleidoscope of activity unfold before my eyes. To appreciate Chicago's diversity, there's no better perch.

Several taxis are in line outside to access the gasoline pumps. Business is heavy tonight, and the banter inside the store remains loud and constant.

A 30-something man files out of his muddied yellow taxicab and enters the store. He's been here before, it seems; he heads directly to a refrigerator in the rear, retrieves a few drinks and hands them to the cashier.

"Busy night, huh?" remarks the

young clerk, noticing the three energy drinks that the man has placed on his counter.

"Busy night," the driver replies as he finishes his purchase, opens a drink,

takes a swig and heads back out into the night.

It's a repeated theme, but not just with taxi drivers. With bar patrons. Couples returning from dates. Students. They're buying energy drinks. Maybe not as much as they're buying soda, beef jerky and M&M's, but enough so that I self-consciously look at my black, decaffeinated coffee and suddenly feel old and out of touch (kind of like when my niece mentions Facebook or Mischa Barton).

"On a busy night, a Saturday night for sure, we're selling tons of Red Bull," says the c-store's night clerk, who prefers not to be identified. "The bars, they bring a lot of the business. But [nonweekend] nights, still, we're always selling [energy drinks]. Teenagers, drivers.

THE BOTTOM LINE

Energy-drink sales have spiked over the past five years, prompting a recent Packaged Facts report to predict the beverage segment will continue to grow annually at 12% with total sales, topping \$9 billion by 2011—a whopping 650% increase from the category's \$1.2 billion in sales in 2002.

Many experts suggest allotting one cooler door for energy drinks and to place it next to sports drinks. Others recommend grouping specific energy SKUs by target audience: supercaffeine, health/wellness, sports.

Very popular.”

It's a buying pattern that affects more than just this eclectic North Side store. Energy-drink purchases are growing exponentially across the country, and retailers are scrambling to sort out the best strategies for leveraging the category's popularity.

Positioning + Location

A recent Packaged Facts report predicted that energy drinks will grow annually at 12% with sales

that will top \$9 billion by 2011, a phenomenal 650% increase from the category's \$1.2 billion in sales in 2002.

These impressive numbers and consumer preferences will play a significant role in buying and retailing decisions. For with this exponential growth has come an onslaught of energy-drink suppliers, all eager to ride the consumption craze.

“C-stores are the single biggest distribution channel for energy drinks,” says Gary

Hemphill, managing director of Beverage Marketing Corp., New York. “As such, it's vitally important that operators give this category its due with ample shelf space and high visibility at multiple locations. ... Finding the proper store location and space allotment is therefore key.”

How many energy drinks should retailers stock and where should they put it? While the specifics are unique to property and location, there are universal strategies to consider.

PERSONAL IMMERSION

I've never been one to follow popular fads, and so this sudden obsession with “energy drinks”—drinking to fuel the body, maintaining efficient metabolic something or other ... well, blah, blah, blah. It all seems just a bit too commercial for me.

And their ingredients? I mean: Caffeine? Taurine? Guarana? Don't try to sell me. I'm a busy adult, I can barely make time to watch four hours of television each night. How do you expect me to sift through the reams of scientific data differentiating between ginkgo biloba and L-carnitine? Whatever happened to just good ol' high fructose corn syrup? But now I'm dating myself, huh?

And so, in an effort to jump full-throttle into the energy-drink phenomenon and finally understand all of the hoopla, I embarked recently on an ambitious consumption experiment: I would attempt to sit comfortably (and passively) on a couch, watching C-SPAN2 in my climate-controlled Chicago apartment while drinking only energy drinks. Would they elevate my alertness? My stamina? My sanity? Here's what I discovered.

6:05 am

There's a presentation of a 2008 budget issue by an Iowa congressman, so I begin by downing two Red Bulls and a Monster. I smile as I lick the ginseng from my lips; both drinks taste surprisingly good. I check the nutrition information, and I feel reassured when I see B12. (I remember seeing that listed on my Frosted Flakes box, too.) I hear the phrase “fiscally prudent middle class” and reach for a second Monster.



First, by “store location,” Hemphill is referring to where retailers position energy drinks within their stores, a mat-

that, breaking the category down by major-brand attributes seems to be the suggested strategy.

“Energy drinks may become the daily vitamin of choice.”

CARA MORRISON

Cogitamus Consulting

ter of determining appropriate adjacencies, a retailing decision that directly affects consumer engagement. And for

“Positioning energy drinks near carbonated beverages and sports drinks may make the most sense,” says Cara Morrison, founder of Cogitamus Consulting and author of the Packaged Facts report “Energy Drinks in the U.S.” “What may be most important is the positioning of brands within the energy-drink cooler space itself. ... Super-

caffeine, for women, health/wellness, sports/activity related, ethnically targeted: Placing like brands together may make it easier for customer purchases.”

Space Allotment

Bevology president Tom Hicks, whose San Francisco-based company produces SuperFly and Zenergize energy-drink tabs, agrees with the brand attribute-grouping strategy; he recommends placing energy drinks near sports drinks. However, he stresses that

6:21 am

Despite the early hour, I’m surprisingly alert. I hear a bird chirping from outside. I count 37 chirps over a two-minute period while a promo runs for Book TV.

8:22 am

Holy cow, it’s difficult sitting still. Not sure how much the segment “Improving Electronic Government” is contributing to my restlessness. I reach for a Full Throttle, and it immediately hits the spot. I begin whistling an obscure country-music tune, sobbing uncontrollably.

11:03 am

I’m digging my newfound heart arrhythmia and flip the channel to C-SPAN2 Espanol. I understand everything, despite never having studied Spanish. I take a swig of Amp and then mute the TV’s sound entirely, supplying my own voice track to a piece that features presenters from the Woodrow Wilson International Center for Scholars. I’m definitely plugged in!

2:40 pm

My restlessness is overwhelming, and even a speech by the Department of Homeland Security’s Michael Chertoff can’t motivate me to focus. I pause when my third-grade teacher enters the room, holding a sign that reads, “Did you return your hall pass?” I always had a crush on Ms. Mattheson, so I’m pleased when she seems attentive as I offer her a sip of XS (I’m on my third). She giggles before whispering, “You were always good at phonics.” As I lean forward to kiss her, I realize that I’m French-kissing my high-def Vizio. My heart is pounding. I must really be embarrassed. Next up: Rock Star.

3:25

What is with my searing abdominal pain? I reach for another Red Bull—my 11th for the day—downing half the can before executing a double backflip and half-Tsukahara on a makeshift vault that I spontaneously build out of dirty socks.

4:55

“Question Time” at the British House of Commons—finally. And it’s all commercial-free! There’s a clip of Gordon Brown. I laugh uncontrollably when I see that they’ve fonted his title as “Labour Prime Minister.” “There’s no ‘u’ in ‘labor’!!!” I scream at my television, without response. Frustrated and without any feeling in my forehead, I race outside and run a respectable 10K while pulling a 2004 Fiat.

11:03

With some assistance from my girlfriend, who handcuffs me to my bedpost (no idea where she got those—wink-wink), I’m ready for bed. My experiment complete, I drink a glass of water, though I don’t feel tired. I break free from the nickel-plated cuffs and rush out onto the wintry Chicago streets, though what happened immediately after that is still a bit hazy.

I awake four days later and discover I’m in a southeastern Dominican Republic resort, wearing SPF 50 clothing and mumbling something about needing to make a la carte restaurant reservations. I head to the bathroom, rubbing the sleep from my eyes, and admire the healthy tan that I’ve somehow acquired. I nod my head, approvingly. Yes, people really *are* on to something, I think. I’m finally understanding the whole energy-drink craze.

I head to the resort’s copious buffet in search of a Red Bull.

store positioning alone is not enough. How much space to allot the category is another concern, a unique consideration that will vary by store and demographic—though patterns are definitely emerging.

"I think right now, you're starting to give it a full door. That's what 7-Eleven is doing," Hicks says. "You see others who are giving it half a door; that's mostly based on knowing their customers. But with the growth of the category—it's approaching \$5 billion [annually]—it deserves a door."

Allotting at least a door is the approach that 35-store c-store chain Honey Farms, based in Worcester, Mass., took in 2007—though it continues to carefully re-examine that figure in an effort to capitalize on its consumers' preferences.

"Each year," says company marketing director Karen Campbell, "we have increased space in [the energy-drink category], and it continues to increase in volume."

Other retailers offer more detailed guidance in their approach to the category, with a strategy that's specific to both adjacencies and allotment.

"In a seven-door cooler set that has

about seven shelves per door, we dedicate four shelves to energy drinks—which equals about 8% to 10% [of the beverage stock]," says retailer Paul Grammer, president of 11-store Circle A Food Mart in Jasper, Ind. "We normally place energy drinks by isotonic drinks—Gatorades and Powerades—and water sections that include flavored waters and vitamin-enhanced waters."

Slipping Sodas

While sales numbers for energy drinks pale in comparison to other nonalcoholic beverages—the Packaged Facts report revealed that energy drinks totaled just 2% of all 2006 nonalcoholic drinks sold (up from less than 1% just two years prior)—the trends for both are notable. "In the past five years," according to the report, "energy-drink sales ... grew at 56% CAGR, while carbonated sodas declined 1%."

The bottom line for retailers: While energy-drink sales seem poised for continued growth, there's a debate whether the popularity will expand the overall consumption base or further erode soda sales.

"We believe that energy drinks are broadening consumption occasions,"

says Hemphill of Beverage Marketing. "Energy drinks satisfy a very specific consumer need: energy. This makes them unique in the overall realm of refreshment beverages, which are generally purchased for [entirely separate reasons]: their thirst-quenching benefits."

While distinct consumption preferences might indeed suggest a broader beverage-category spike, it's hard to ignore the bottom-line numbers (see sidebar, p. 65). And recognizing that, the cannibalization effect seems obvious.

"Any time a new product or category comes out," Hicks says, "you would hope that it increases consumption of the overall category. But look at the numbers; it's clearly cutting into other beverages, especially soft drinks."

Others insist that energy drinks are both increasing the consumption base *and* eroding soda sales.

"The segment they are going after is the younger 18- to 25-year-old male crowd," says Grammer. "[But] we also see young women buying these drinks. Energy drinks seem to be selling in all day-parts. ... The segment of drinks that has been shrinking is the carbonated drinks, so naturally some have migrated over to the energy-drink section.

"People who are looking for the burst of energy or to stay awake who do not like coffee seem to be experimenting with this category," he continues. "The 20- to 30-something generation seems to always be looking for that different kind of drink that does more for them. They do not want to drink what Mom and Dad drink. They want their own drinks."

2008 BEST BETS

Bump Williams, general manager of Chicago-based Information Resources Inc.'s beer, wine and spirits practice, cites the following drinks and trends to watch in 2008.

Soda: "Low-cal or no-cal drinks will continue to grow in this category. Health and wellness are growing concerns."

Energy Drinks: "Both Red Bull and Monster will see double-digit growth in 2008. Monster especially, because of its [Anheuser-Busch] relationship."

Sports Drinks: "The jury is out. G2—the new Gatorade drink for nonathletes—is one to look for. And Gatorade is also coming out with a low-cal version."

Waters: "This is a tough one," he says, before hedging his guess. "I think we'll see a high-end—something Fiji-like—and a low-end emerge."

Teas: "Flavored teas will rise, and high-ends will also emerge."

Still others concede that while soda sales are slipping, it's not solely related to competition. "The flight from sodas is heavily influenced by a general trend toward health and wellness," Morrison says, "and not necessarily as a direct result from the rise in energy drinks."

Selecting Inventory

With a rush of suppliers trying to squeeze into an already busy marketplace, making sense out of a crowded field can be difficult for retailers.

"I walked into a buyer's office in Idaho the other day," says Hicks, "and he had 360 different energy drinks. His whole office was lined with different brands. Like any category, it gets crowded quickly and that's what's happening now." His advice? "Retailers need to make sure that they bring in brands with proper marketing support."

While selling name brands is a sound strategy, it's crucial to know what each store's customers want.

"When making shelf decisions, be sensitive to the makeup of your community," Morrison advises. "Is the population largely young families? [If so], consider stocking health-focused energy drinks for women such as Go Girl or Tab Energy. Perhaps there is a large Hispanic community. If so, perhaps stock Caballo Negro or Blue Demon."

For retailers experienced selling energy drinks, the advice seems logical. But for those treading head-first into the category for the first time, the approach can seem daunting. Morrison insists the challenge need not be overwhelming.



"First off, use the eyes," she says. "Most c-store proprietors and managers should have enough awareness about their local community to make this type of call. If part of a larger franchise, proprietors should make use of any resources the mother ship has to offer in terms of quantitative and qualitative research."

And if none of the above apply?

"Check local census data," Morrison says. "Or if the business wants to lay out some money and time, they could do some consumer 'profiling' or track the number of consumers entering the store over a given period."

More generally, though, many retailers are already identifying general purchasing trends, irrespective of demographics.

"Monster Java has been ... flying off the shelves," says Grammer of Circle A Food Mart. "This is a hybrid of coffee

COMMON ROOTS

Despite the retail distinction today between carbonated soft drinks and energy drinks, both share common promotional histories. Many energy drinks are positioning themselves much as carbonated drinks did during the category's launch in the late 19th century: Not just beverages, but *functional* beverages—drinks that promote good health. According to Packaged Facts, energy-drink manufacturers are "incorporating nutrition, pain-killing and anti-aging ingredients into their products," elixir-like qualities not unlike those that the carbonated-beverage industry promoted during its nascency.

When it was developed in the late 19th century, Coca-Cola was touted as a health drink, able to cure ailments such as impotence and headaches. Print ads from the early 20th century used terms such as "revives" and "sustains" when promoting its benefits.

Ironically, Coke's curator, John Pemperton—the product's staunchest promoter of its healthful benefits—provided conflicting testimonial support to this claim: He died less than two years after creating the drink.

But while energy drinks market a range of benefits, industry insiders still point to "added energy" as the category's most popular draw.

"Americans work hard and they're tired. We're always looking for an extra boost, something to give us an edge," says Bevology president Tom Hicks, whose San Francisco-based company produces SuperFly and Zenergize energy-drink tabs. "It's the nature of America. We're the hardest-working people on earth."

Shock Coffee president Jeff Rosen agrees. "We've become a 24/7 society [requiring] more hours per day, and the easy way out is to perk yourself up with a quick fix from an energy drink," he says. The point receives personal significance for him: "Here I am at 11:30 p.m. on a Friday night working when I should be in bed watching Jay Leno."

Paul Grammer, president of Circle A Food Mart, an 11-store chain based in Jasper, Ind., agrees, though he cites taste as an additional factor. "People [who] didn't like coffee but wanted the caffeine boost turned to energy drinks," he says.

and energy. Hybrid drinks seem to be the hot items. There are now also energy-shot drinks that are becoming popular. ... These drinks do not even have to be in the cooler but can be on the front counter as an impulse item."

This differentiation of the energy-drink category is not surprising, especially when the consumer pool is so large—and growing.

"The market for energy drinks is in a state of flux with new-product inno-

vation and introduction,” says Morrison. “New companies are constantly trying to [break] into the market, hoping to come up with the next big thing in energy.”

100% Risk-Free Guarantee?

With industrywide data supporting predictions that the energy-drink category will continue to rise, most see the retailing risks for retailers as minimal. They point to the category’s young history and urge experimentation to best discover new retailing opportunities.

“This segment is still growing, so if you want to be in this segment, you have to try the new flavors that come out, the new sizes, and see what sells,” says Grammer. However, he concedes such a strategy carries risks.

“[Energy] drinks also carry a higher price tag, which can also tie up inventory dollars quick[ly] if they do not turn. But along with that, they also sell at a higher price point, which helps your average ticket transaction.”

However, overinvestment is still fraught with uncertainty, especially when retailers drift from their core strengths, cautions Shock Coffee president Jeff Rosen. Thinking of producing your own energy drink—maybe *Orange Bull*? Think again. Start-up costs make such a proposition financially tenuous at best.

“We’re seeing a greater trend in c-stores crossing over into the brand-

ing business,” Rosen says. “Branding your own energy drink takes a good deal of funding, which definitely makes it a risky business. ... The start-up costs can easily exceed \$100,000, not to mention the advertising and time it takes to be successful. In the end a brand with national recognition will far outsell a local or regionalized brand.”

The Future

Most see the opportunities and immediate future for the energy-drink category as bright. “I think it’s going to see tremendous growth for 2008 and beyond,” says Hicks. However, whether it will remain positive long-term is another issue.

Some consumer watchdog groups have voiced concerns that energy drinks should have an age requirement akin to that of alcohol and tobacco. They advocate limits on the amount of caffeine and other additives in the drinks. Their basic concern is that energy drinks will create physiological highs and lows and, thus, should contain warnings for drinkers who may not be well-suited to consume them.

“The category is so new—less than 10 years old—that we don’t understand the impact of heavy consumption,” he says. “If negative health risks start surfacing, who knows? I have a friend with an 18-year-old who had a heart attack. We don’t know why, but he drinks a lot of energy drinks.”

“The 20- to 30-something generation seems to always be looking for that different kind of drink that does more for them. They do not want to drink what Mom and Dad drink. They want their own drinks.”

PAUL GRAMMER *Circle A Food Mart*

Circle **XXX** on page **XX**
for product information

March 2008

CSP

63

LEADING THE PACK

While Red Bull sits comfortably atop the energy-drink category, competitors are gaining ground.

| Top U.S. Energy-Drink Brands (\$ millions) | 2002 | 2003 | 2004 | 2005 | 2006 | CAGR | % Share |
|--|------|------|-------|-------|-------|--------|---------|
| Red Bull | 57.4 | 91.3 | 156.1 | 225.8 | 271.9 | 47.5% | 43% |
| Monster Energy | 0.7 | 5.0 | 16.4 | 45.0 | 91.2 | 236.7% | 14% |
| Rockstar | 4.3 | 10.2 | 23.1 | 43.5 | 72.3 | 103.1% | 11% |
| Full Throttle | NA | NA | 0.2 | 23.0 | 44.1 | NA | 7% |
| SoBe No Fear | NA | 3.5 | 10.1 | 20.1 | 34.4 | NA | 5% |
| Amp | 11.5 | 12.4 | 14.2 | 19.9 | 23.1 | 19.1% | 4% |
| SoBe Adrenaline Rush | 12.0 | 13.2 | 15.2 | 21.2 | 18.4 | 11.3% | 3% |
| Tab Energy | NA | NA | NA | NA | 14.3 | NA | 2% |

Source: Information Resources Inc., compiled by Packaged Facts. Includes mass merchandisers (excluding Wal-Mart), U.S. supermarkets and drug stores.

So what's next? "Energy drinks with added nutrition—vitamin C, for example—will be the next step," Hicks predicts. "To claim that your drinks boost energy while providing nutrition, that's already catching on."

It's no surprise, Morrison says.

"Nanotechnology and microencapsulation may grow the user base of energy-drink innovation. ... Its ability to mask additive flavors means that supplements such as omega-3 can be included without altering the flavor of a beverage."

The end result for consumers: "Energy drinks may become the daily vitamin of choice," Morrison predicts. "Don't be surprised to see crossover from the vitamin, mineral and supplement [worlds]."

"Centrum Energy Drink, anyone?" ■