

BELUGA GROUP

Taste in Good spirits

► **We initiate coverage of Beluga Group (MOEX: BEGU), the leading Russian alcohol producer and important global market player.**

Beluga Group is the number one Spirits producer in Russia and ranks as a top-four vodka producer globally. It manages a portfolio of own and imported alcohol brands. Beluga Group had a 12.5% share in spirits production in Russia in 2019 and was Russia's number one alcohol company by production volumes. The company's activities include alcohol production and distribution, retail operations, and also food production. The Group entered the wine segment with its own premium wine brand after acquiring the Golubitskoye vineyard with its over 2mn bottles capacity in 2018. The development of the Winelab alcohol retail chain provided a distribution channel for the Group's own and importer partners' brands in three regions, including Moscow, St Petersburg and North West, Far East. The retail chain consisted of 604 stores at the end of 2019. Beluga Group's revenue and margin drivers include increased Beluga vodka brand sales and exports, growth of imported brand sales in Russia, own wine sales and the ramp-up of the retail operations after the intensive program of new openings in 2018-2019. The focus on premiumization and diversification has allowed the Group to maintain a healthy operating margin while also growing sales volumes. In 2019, the Group achieved RUB53.1bn of revenue, up 22% YoY, and RUB5,299mn EBITDA before IFRS 16, up 25% YoY and EBITDA at RUB6,495mn after IFRS 16. Net income was RUB1,433mn, up 53% YoY. The Group's buyback program will result in the cancellation of a 19% stake, cutting the number of shares outstanding to 15.8mn, which includes 3.2mn treasury shares. In 1Q19, the group reported 19% YoY volumes growth to 3,201k 9L cases and 'steadily high demand' for 2Q20 deliveries.

► **Attractive market: Russian alcohol output has grown by 3.1% in 2015-19, driven by local demand and a pick-up exports volume. Retail sales volumes remain steady YTD.**

Despite global declining total pure alcohol per capita consumption, Russian alcoholic drinks producers increased their production volumes, benefiting from an attractive cost curve, product diversification and regional and international brands development. The alcoholic drinks market represented an over \$1.5 trln opportunity globally in 2019, including over \$44bn for vodka, \$68bn for brandy, \$86bn for whisky and \$315bn for still wine. The growth of the market may reach a 3.5% p.a. CAGR in 2020-2023. The COVID-19 breakout disrupted Global Travel Retail and the 'out-of-home' channel. However, Russian domestic alcoholic drinks sales are steady, according to producers. Russia is the world's #1 market by vodka consumption, but also an attractive wine market for local producers and importers. Russian wine consumption is growing due to lifestyle changes, healthier drinking choices by customers, and higher income per capita. We believe that growth in the Russian alcoholic drinks market (excluding beer, cider, perry etc.) will be at least 2.6% p.a. in the medium term, despite a decline in pure alcohol consumption per capita. This represents growing opportunities of over 2.4% in vodka, 3.3% in cognac, 2.8% in wine, and 3.9% in liqueurs for local and international players.

Beluga Group has a unique market position in Russia and will benefit from strong brand recognition globally.

The company has established a strong position as a producer and distributor of spirits and wine in Russia, while its exports of the super-premium Beluga vodka brand have grown at over 20% p.a. in 2018-2019. The focused sales efforts and further brand portfolio diversification will result in 7.8% p.a. revenue growth in 2019-2025. We expect the company to keep its capex low and to focus on operational improvements in its retail operations and vineyard. The debt position remained relatively comfortable at 2.6 Net debt/EBITDA before IFRS 16 at end-2019. We have valued Beluga Group on a 12-month fair market capitalization, using a DCF approach, of RUB27.8-36.9bn that translates into RUB2,208-2,926 per share, based on 12.6mn shares outstanding. Risks include the impact of COVID-19 on Global Travel Retail, the negative effect of ruble devaluation, competition from cheap local brands and a deceleration of sales growth in premium/super-premium segments.

Report date:	16 April 2020
Ticker	BEGU
Main exchange	MOEX
Current Price, RUB	1,482
Number of shares issued	19,400,000
Number of shares outstanding	12,610,000
Treasury shares	6,790,000
Treasury shares after cancellation*	3,190,000
Current MCap, RUB mn	18,688
Free float current, %	14%
Free float after cancellation*, %	17%

*) subject to cancellation of 3.6mn treasury shares

BELUGA Group is one of the largest companies in Russia's alcohol market. The Group operates a portfolio of own and imported brands, producing and selling top-quality alcohol in the spirits and wine segments. The Group controls c. 11% of vodka and 12% of brandy production in Russia and 20% of flavored liquors output. The Group's brand Belenkaya is a top-20 bestselling vodka brand globally. The Group's key brands are vodkas Beluga, Myagkov, Belenkaya, Arkhangelskaya, Tsar, Snow Owl and, Copper Horse; sparkling wine Vogue; and brandies Golden Reserve and Bastion. The Group's products are sold in over 90 countries.

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#1 Spirits producer in Russia



Strong distribution platform in Russia



Diversified portfolio of own and imported brands



#4 Vodka player globally



EBITDA margin 12.2% in 2019



Revenue 5-year CAGR 13.5% in 2014-2019

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Investment summary

1. Market opportunity

The alcoholic drinks market represented an over \$1.5 trln opportunity globally in 2019, according to Statista. Market growth may reach 3.5% p.a. CAGR in 2020-2023, once the market recovers from the COVID-19 impact. Average alcohol revenue per capita was estimated at \$202.4 in 2019. The alcoholic drinks market experienced some decline in developed markets in volume terms while emerging markets are still growing. The value growth is driven primarily by premiumization and by the growth of the out-of-home segment. Worldwide, over 40% of money spent on alcoholic drinks were for consumption out of home, at venues including bars, cafes, and restaurants. The proportion of out-of-home spending is expected to continue to grow to 44% by 2023, proving the importance of on-trade sales channels for the industry. The online sales channel is growing, with an estimated 1% of consumer spending on food, drink and tobacco products to be attributed to online retail by 2023. The average pure alcohol volume consumed per person was estimated to amount 40.2L in 2020 before coronavirus outbreak, from the four segments as beer, spirits, wine, and cider, perry& rice wine.

The spirits segment, the second-largest segment of the alcoholic drinks market by revenue after beer, may deliver the greatest growth in the sector, at an estimated 3.2% CAGR 2020-23, from revenue of \$443bn in 2019. The volume of the global spirits market was estimated at 33bn litres in 2019, with average revenue per capita estimated at \$58 and the average per capita consumption globally at 4.4L. The spirits segment includes several major sub-segments: whiskey, vodka, rum, gin, brandy and liqueurs & other spirits.

The coronavirus outbreak has affected alcoholic drinks companies in a number of ways:

- The out-of-home segment of the market, which may represent up to 50% of some producers' revenues, will likely take a major hit due to the 'stay-at-home' policies in place in the largest markets.
- Global Travel Retail sales have shrunk due to the suspension of air travel.
- Alcoholic drinks distribution has shifted from the out-of-home to the 'e-commerce' and 'at-home' channels.
- Spirits producers are increasing their drinks storage and focusing on supporting their communities and distributors, including bartenders.

The Russian spirits market grew at a 3.1% CAGR between 2014 and 2019, including 6.9% growth in the vodka segment. Russia is one of the largest vodka markets, with consumption exceeding 92mn 9L cases per year. Despite declining alcohol consumption per capita over the last 15 years, Russian alcohol consumption in value terms has been supported by changing consumer preferences in favor of premium spirits and wines. Russia's wine segment is growing faster than the spirits segment due to changing personal income, healthier lifestyle choices, increasing out-of-home consumption of alcohol, and an increasing variety of drinks on the local market. The sales of alcoholic drinks in Russia were 202mn dal in 2019, having grown at a 5.1% CAGR in 2017-19. Being a large alcoholic drinks exporter, Russia is expanding its distribution globally, including its Global Travel Retail business and regional chains. The top three Russian spirits producers are Beluga Group, Roust, and Tatspirom with Beluga Group being the number one by volume in 2019.

The 'out-of-home' channel still accounts for a very limited share of the Russian alcoholic drinks market, reaching just 2-3% for some producers. This means that COVID-19 will likely have a limited impact on domestic sales. In March 2020, Russian alcoholic drinks producers and distributors reported strong sales growth as the government's 'stay-at-home' policy

prompted an increase in alcoholic drinks sales. The industry may pay the price later; however, for now domestic alcoholic drinks sales are ahead of last year.

There are several long-term trends in the Russian alcoholic drinks market:

- Reduction of the 'grey' market following the mandatory marking with a unique code of all alcohol bottles produced.
- Increasing variety of the offering of alcoholic drinks on domestic market.
- Increased share of wine in the alcoholic drinks market.
- Consolidation in the sector.

2. BELUGA Group

Beluga Group (MOEX: BELU) is the leading alcoholic drinks industry player in Russia. The company has a strong brand portfolio, including the globally well-recognized super-premium vodka brand Beluga. The Group operates in two main business areas Alcohol and Specialized Alcohol Retail. The Alcohol segment includes the production of own brands at seven production facilities across Russia as well as the bottling of partner's brands, such as William Lawson's Bacardi. The Group also manages a nationwide distribution of a portfolio of imported brands, including important global names such as William Grant & Sons, Camus cognacs, Torres brandy, Barcelo rum. The portfolio of own brands includes Beluga super-premium vodka, and its other vodka brands Belenkaya, Myagkov, Arkhangelskaya, Snow Owl, Copper Horse, along with other spirits brands Golden Reserve, Bastion, Tiflis Treasure, Trouble Maker, Le Lion de Pierre, Eagle's Rock and Green Baboon. The imported wine portfolio includes wines from well-recognized global wine houses including Cono Sur, Torres, Masi Agricola, Frescobaldi Group, and Domaines Baron de Rothschild. The spirits that Beluga imports include such names as Grant's, Glenfiddich, Clan MacGregor, Monkey Shoulder, Torres, Milagro and Barcelo. Beluga Group's marketing efforts are focused on distribution of premium brands and products, to generate an extra-margin on the Russian market which is already saturated with cheap vodka offerings. The strategy focused on premiumization, diversification of brand portfolio by price category and by spirit segment helped the Group to maintain good revenue growth in the spirits segment between 2014 and 2019. In 2018, the Group acquired the Golubitskoye vineyard with capacity of over 2mn bottles to develop an own premium wine brand in both the still wine and sparkling wine categories.

Since 2018, the Group is intensively developing the retail chain Winelab and increased the number of stores to 604 in 3 major regions by the end of 2019. The company is going to open up to 400 new stores between 2021 and 2026. The retail business allows Beluga Group to increase the market penetration with own and imported brands as well as focus marketing efforts more effectively on distributed brands.

There are several drivers of the company's total revenue growth and margin improvement: growth of Beluga vodka brand sales and exports, growth of imported brands sales in Russia, the own wine sales expansion, and a ramp-up of the Retail segment operations following intensive new openings in 2018-2019. The focus on premiumization and diversification allows the Group to maintain a healthy operating margin while growing sales volumes. The Group reported RUB53.1bn revenue for 2019, up 22% YoY, RUB5,299mn EBITDA before application of IFRS 16 (up 25% YoY) and RUB6,495mn EBITDA after IFRS 16 (up 53% YoY), with net income RUB1,433mn, up 53% YoY. The group reported RUB15.0bn debt and RUB13.9mn net debt, putting net debt/EBITDA at 2.6x based on EBITDA before IFRS 16 as of end 2019. The operating margin reached 10.1% in the Alcohol segment, 3.8% in Retail

and 0.8% in Food segments, and the promising ramp-up in Retail segment and wine sales expansion should drive a margin increase in the future.

The Group's buyback program will result in the cancellation of 3,600 thousand shares, cutting the number of shares issued to 15.8mn. The stake of 3.2mn treasury shares will remain available for the Group's further capital decisions, including potential M&A and secondary offerings. The adjusted number of shares outstanding will be c12.6mn.

The company's share price performance was supported by strong operating results in 2018-2019 and the share buyback program. The share price grew by 80% in 2019 and has risen by 67% YTD.

Pros

- Strong market position in its key segments and good diversification of its operations.
- Strong portfolio of brands, including brands in the super-premium and premium segments.
- Growth of super-premium and premium segments in Russia and internationally.
- Dominant market position in the vodka category in Russia.
- Large scale of operations in Russia.
- Beluga Brand's global recognition supports growing exposure internationally, including the Global Travel Retail.
- Potential M&A opportunities in Alcoholic Drinks market.
- Large production capacities.
- Potential expansion of operations in the wine segment and own wine brand development.
- Tax privileges for grape and wine producers in Russia.
- Strong management and partners.

Cons

- COVID-19 will negatively affect the Global Travel Retail business and the 'out-of-home' consumption in 2020.
- The recent oil price drop has resulted in Ruble devaluation, causing a potential risk for inflation and macro trends deceleration in Russia.
- The global suspension of travel and constraints on economic activity will result in lower economic growth, lower disposable income and potentially lower demand for premium products in Beluga Group's segments.
- The competition of local producers in the lower price segment and falling consumer confidence may all result in a domestic market decline in higher price alcoholic drinks segments.
- Increased competition on selected routes may affect the freight rate negotiations.

3. Valuation summary

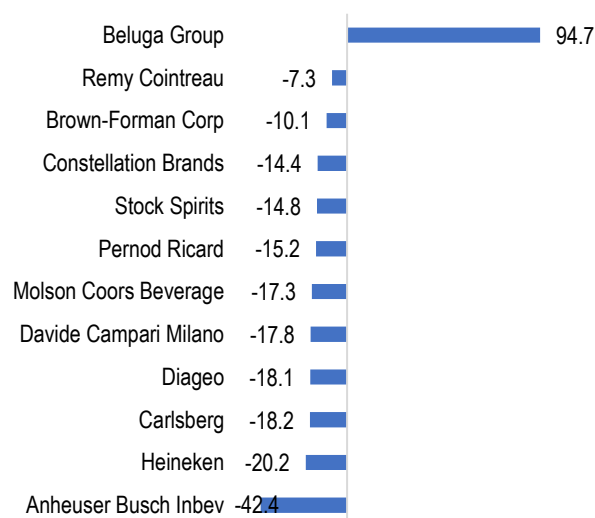
We have valued Beluga Group shares based on an FCFF approach. Our DCF model provides the valuation range for a 12-month fair market capitalization of RUB27.8-36.9bn. The company's shares trade at 4.2-4.6 EV/EBITDA based on 2020-21 estimates and 6.1-8.0 P/E. The global spirits producers' multiples for 2020-21 are 16.3-17.9 for EV/EBITDA and 25.0-28.1 P/E.

The company has a very small number of peers due to its size and the industry classification. The Russian universe includes mostly consumer and retail companies.

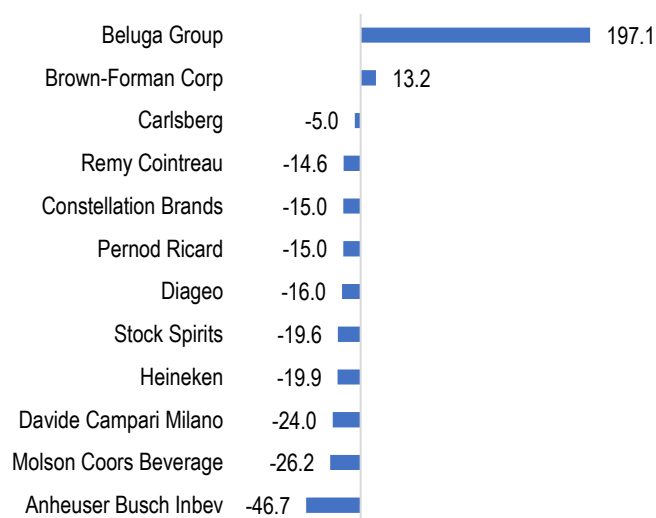
Figure 1. Comparable multiples for consumer and alcoholic drinks peers

Company name	Market Cap., \$mn	EV, \$mn	P/E Fwd 1Y	P/E Fwd 2Y	P/E Fwd 3Y	EV/ EBITDA 1Y fwd	EV/ EBITDA 2Y fwd	EV/ EBITDA 3 fwd	EV/ Revenues 1y fwd	EV/ Revenues 2y fwd	EV/ Revenues 3y fwd
Beluga Group	254	443	8.0	6.1	4.9	4.6	4.2	3.9	0.5	0.5	0.5
<i>Discount to Global peers</i>			-67%	-71%	-73%	-69%	-69%	-69%	-86%	-86%	-87%
<i>Discount to Global Spirits peers</i>			-71%	-75%	-77%	-74%	-74%	-74%	-90%	-90%	-90%
<i>Discount to Russian Consumer and Retail</i>			-68%	-71%	-71%	-48%	-47%	-48%	-26%	-24%	-23%
Global Alcoholic Drinks sector											
Diageo PLC	77296	94381	23.0	21.6	17.9	18.6	16.6	15.3	6.2	5.8	5.5
Pernod Ricard SA	39384	47985	25.6	21.3	18.4	17.6	15.4	13.9	5.1	4.8	4.5
Anheuser Busch Inbev NV	77893	182436	18.6	13.2	12.2	10.4	9.5	9.2	4.0	3.6	3.6
Heineken NV	47885	65453	22.1	17.5	15.9	12.4	10.9	10.2	2.8	2.5	2.4
Remy Cointreau SA	5589	5944	43.6	41.5	34.2	23.6	23.3	20.3	5.4	5.4	5.0
Carlsberg A/S	18574	21815	22.3	18.1	16.3	11.0	9.8	9.2	2.4	2.3	2.2
Davide Campari Milano SpA	8529	9124	34.4	26.5	22.9	20.1	17.1	15.5	4.8	4.3	4.0
Molson Coors Beverage Co	9728	18496	13.4	12.7	11.7	9.1	8.8	8.7	1.9	1.8	1.8
Brown-Forman Corp	28300	30321	35.5	39.6	33.8	25.9	25.1	24.7	9.0	9.7	9.2
LVMH Moët Hennessy Louis Vuitton SE	189629	210863	30.0	22.9	20.6	14.6	12.0	11.1	3.9	3.4	3.2
Constellation Brands Inc	30957	43402	19.2	16.8	14.4	15.1	14.1	12.9	5.6	5.4	5.1
Heineken Holding NV	22183	48814	17.7	15.5	14.7	8.4	7.4	7.1	2.0	1.9	1.8
Boston Beer Company Inc	5103	5069	41.7	32.6	26.0	20.4	16.7	14.3	3.4	2.9	2.4
Royal Unibrew A/S	3503	3878	23.1	19.7	18.7	16.1	14.2	13.8	3.6	3.4	3.3
C&C Group PLC	785	1154	7.8	10.0	7.6	8.1	9.4	8.3	0.6	0.7	0.7
Stock Spirits	444	487	13.5	10.2	9.6	7.2	7.2	6.8	1.4	1.4	1.3
Average			24.5	21.2	18.4	14.9	13.6	12.6	3.9	3.7	3.5
Global Spirits average			28.1	25.0	21.5	17.9	16.3	15.1	5.2	5.0	4.7
Magnit PAO	4426	11546	17.9	15.6	12.9	6.1	5.3	5.0	0.6	0.5	0.5
X5 Retail Group NV	7560	16670	15.8	14.5	12.3	6.7	6.7	5.3	0.6	0.6	0.5
Lenta Ltd	961	2401	12.4	8.3	7.5	4.7	4.7	4.8	0.4	0.4	0.4
O'Key Group SA	171	854	8.3	9.2	9.5	4.7	4.5	4.4	0.4	0.4	0.4
Detskiy Mir PAO	967	1644	8.6	7.7	7.4	6.9	6.0	5.1	0.8	0.8	0.7
Eurocash SA	677	1252	23.0	18.4	13.7	9.9	9.2	5.9	0.2	0.2	0.2
Sok Marketler Ticaret AS	880	1106	68.8	28.7	18.6	4.7	3.7	3.5	0.4	0.3	0.3
Dino Polska SA	3962	4099	30.4	23.8	19.4	18.1	14.5	11.7	1.7	1.4	1.1
BIM Birlesik Magazalar AS	4825	5138	23.1	18.2	15.3	9.6	8.1	7.2	0.7	0.6	0.5
Migros Ticaret AS	767	1506	NaN	31.1	NaN	4.4	3.8	3.9	0.4	0.3	0.3
LPP SA	2546	3140	20.3	27.9	17.6	8.5	9.3	9.2	1.4	1.5	1.2
Ros Agro PLC	1100	2107	8.8	7.8	7.2	8.2	7.2	7.2	1.1	1.0	1.0
CCC SA	466	1227	16.1	9.7	8.5	6.1	4.8	4.5	0.9	0.7	0.6
Shoprite Holdings Ltd	3967	5220	18.3	17.7	16.6	7.5	7.3	7.0	0.6	0.6	0.5
President Chain Store Corp	9900	11144	26.8	25.1	23.0	13.4	13.0	13.0	1.3	1.2	1.1
GS Retail Co Ltd	1946	4502	14.9	12.1	12.1	6.9	6.9	7.0	0.6	0.6	0.5
Pick N Pay Stores Ltd	1588	2431	19.2	18.0	16.7	7.3	6.9	6.6	0.5	0.5	0.4
BGF Retail Co Ltd	2075	2163	15.9	14.1	13.6	5.6	5.2	6.4	0.4	0.4	0.4
Grupo Comercial Chedraui SAB de CV	993	2320	9.6	8.7	8.7	5.8	5.5	5.0	0.4	0.4	0.4
Sumber Alfaria Trijaya Tbk PT	2216	2254	25.5	21.7	16.7	9.0	8.7	7.6	0.4	0.4	0.4
Taiwan FamilyMart Co Ltd	1643	2188	24.3	21.5	20.1	9.1	8.4	11.2	0.8	0.7	0.7
Jiajiayue Group Co Ltd	2790	2583	43.7	36.4	29.5	21.7	18.0	15.2	1.2	1.0	0.9
La Comer SAB de CV	402	358	22.2	20.0	NaN	3.8	3.4	2.7	0.4	0.3	0.3
7-Eleven Malaysia Holdings	387	539	22.3	23.4	21.5	8.1	8.3	8.2	0.9	0.9	0.8
Russian peers average			12.0	10.5	9.5	6.2	5.7	5.3	0.7	0.6	0.6
Consumer and retail average			25.0	20.9	17.0	8.9	8.1	7.5	0.7	0.7	0.6

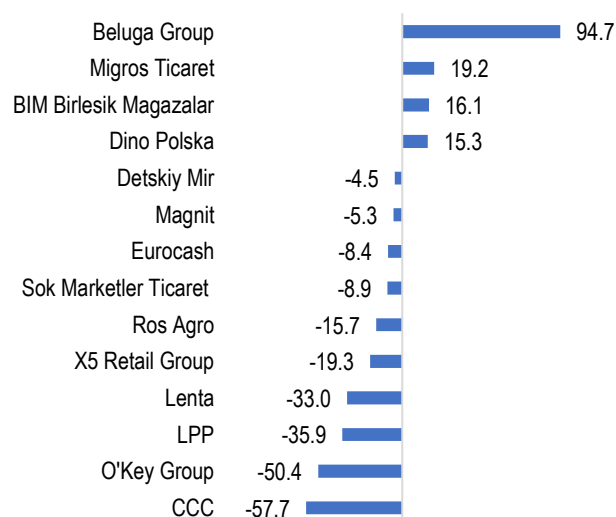
Source: ThomsonReuters, Hypothesis Research estimates

Figure 2. Performance of alcoholic drinks peers YtD

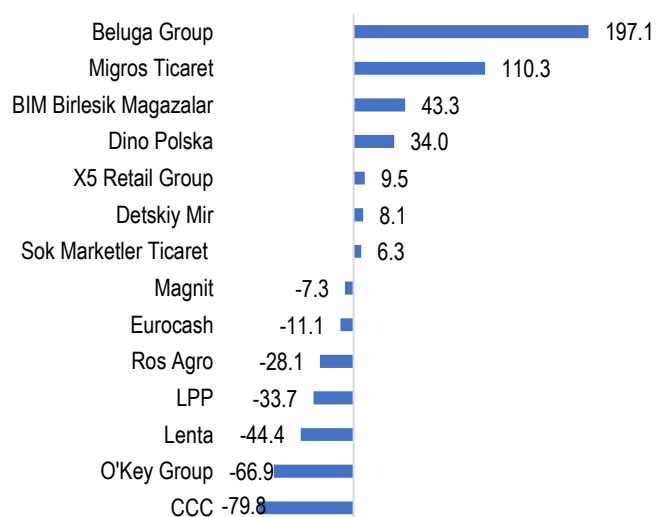
Source: ThomsonReuters

Figure 3. Performance of alcoholic drinks peers 1Y

Source: ThomsonReuters

Figure 4. Performance of consumer and retail peers YtD

Source: ThomsonReuters

Figure 5. Performance of consumer and retail peers 1Y

Source: ThomsonReuters

The Global Alcoholic Drinks Market

The global alcoholic drinks market size for 2019 is estimated at \$1.5trln by Statista. The market growth forecast before the corona virus outbreak was a 3.5% p.a. CAGR for 2020-2023. The market is broken down into four segments: beer, spirits, wine, and cider, perry & rice wine. Beer is the largest segment in terms of revenue, with an estimated \$592bn in 2019, while the spirits segment reached \$443bn, wine \$370bn and cider, perry & rice \$128bn in 2019. The average alcoholic drinks market revenue per capita is estimated at over \$200 in 2019.

COVID-19 impact

COVID-19 will likely have an impact on companies in the alcoholic drinks market. The leading companies in the segment have made the following statements:

- Pernod Ricard announced that Travel Retail may see an 80% business decline for the period from February to end-June. The company had very limited business in February and March and expects a slow recovery from April in China. Off-trade business may see a c.10% sales reduction from mid-March to end-June, while on-trade will have no sales from mid-March to end-June, as outlets are shut and not reordering. The combined impact will likely lead to an organic decline in profit from Recurring Operations of -20% for FY2020.
- Davide Campari-Milano reported that the on-premises channel has been strongly impacted by the travel and social restrictions in the group's key markets, while the off-premises channel should suffer less of an impact. At the same time, all of the group's plants and distilleries are operational as of the end of March 2020.
- Diageo is pledging £1mn to support bartenders in the free trade across Great Britain alongside other measures to support customers. The group provided a guidance including some 2.3% negative effect on revenue in February 2020. However, the impact from the spread of COVID-19 in Europe and the US will likely be greater.
- Amheuser Busch InBev stated in February that it expects a significant decline in demand in the on-premises channels, including night-life and restaurants, mostly in China. The group has relocated its resources, where possible, to the in-home channels and e-commerce.
- Beluga Group and a number of other Russian alcoholic drinks producers and distributors recorded an increase in alcoholic drinks sales in March 2020. The limited 'out-of-home' share of alcohol sales in Russia makes the Russian market less exposed to the negative effects of lockdowns.

We do not believe that the initial forecasts of c. 3.5% p.a. growth in the alcoholic drinks sector this year will be realized as all major channels have been affected by lockdowns globally.

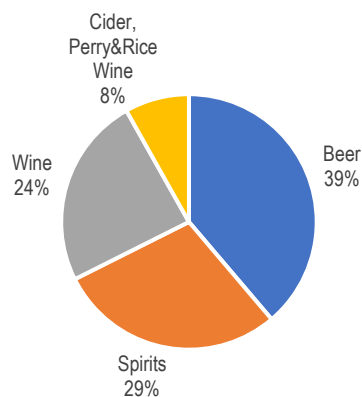
- Travel Retail will lose at least two to four months of revenues due to the suspension of travel and flights to all major destinations. Once the lockdowns are lifted, we expect the recovery in the segment to take until the end of 2020.

- The out-of-home channel will lose between two and five months of revenue due to governments' 'stay-in-home' policies. The US market has been heavily affected by the spread of coronavirus, making any estimates unjustified.
- The industry is trying to re-allocate distribution from the 'on-premises' channel to the 'at-home' and 'e-commerce' segments.

According to Diageo estimates, 6bn equivalent units of alcohol are sold each year with total retail sales of £747bn (\$956mn). There are 550mn new consumers expected to enter the market by 2030, having reached the relevant legal purchasing age. Diageo also expects that 750mn of consumers will be able to afford international-style spirits over the next ten years, according to Diageo. The growing global population, increasing income per capital in developing world and changing preference form the trend of the global alcohol market.

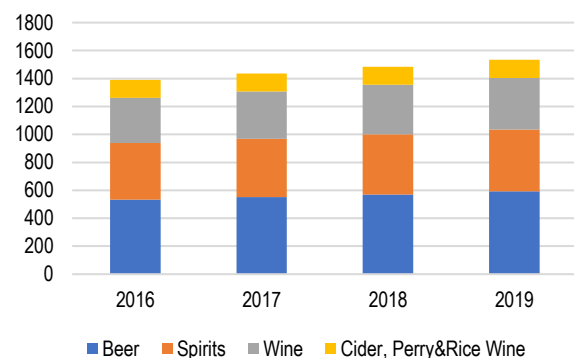
The alcoholic drinks market has been declining in developed markets by volume; however, the global market has been supported by emerging markets growth. The value growth is driven primarily by premiumization and by the growth of the out-of-home segment. Worldwide, over 40% of money spent on alcoholic drinks is for consumption out of home, including bars and restaurants. Out-of-home is expected to increase to 44% of total spending in 2023. On-trade sales channels are very important for the industry. The online sales channel is growing with an estimated 1% of consumer spending on food, drink and tobacco products to be attributed to online retail by 2023. The global average alcohol volume per person in 2019 was earlier estimated at 40L across the entire market which includes beer, spirits, wine, cider, perry& rice wine.

Figure 6. Global alcoholic drinks market, \$bn by segment 2019 estimates



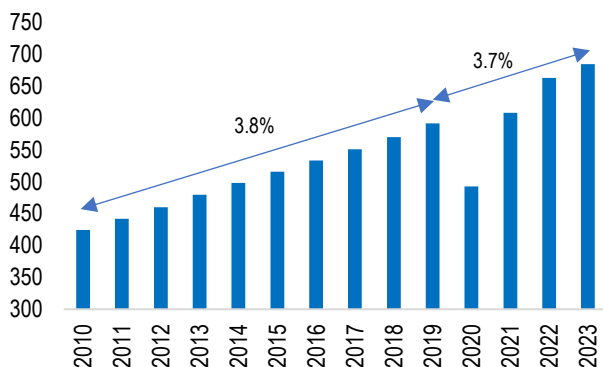
Source: statista.com

Figure 7. Global alcoholic drinks market, \$bn by segment dynamics

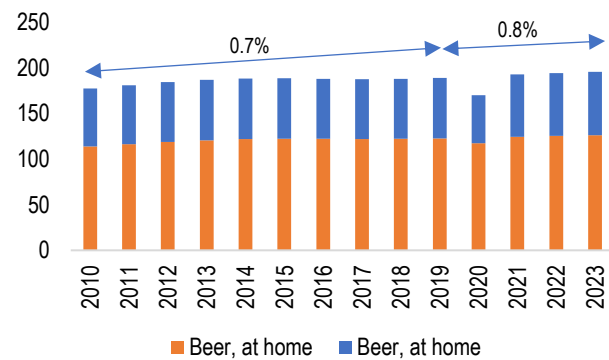


Source: statista.com

Beer is the largest segment of the Alcoholic drinks market by both volume and by value. Beer includes fermented beverages made from malt with an alcoholic content of over 0.5% and also beer mix drinks (non-alcoholic beer is not included in the segment). The estimated revenue in the segment is \$592bn for 2019 and the average revenue per person is \$78. The segment is quite concentrated, with the top five players, Anheuser-Busch InBev, Heineken, China Resources, Carlsberg, and Molson Coors, controlling c 60% of the global volume, and the leader AB InBev accounting over 30% of the volume alone. The essential revenue, estimated at \$118.4bn, is generated in the US.

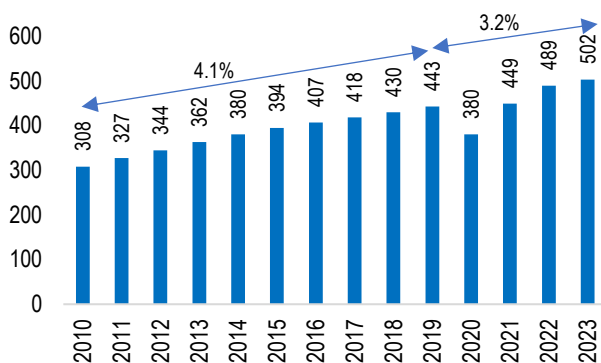
Figure 8. Global Beer market, \$bn

Source: statista

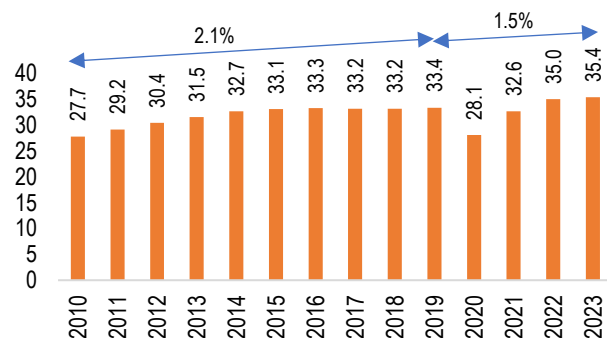
Figure 9. Global Beer market volumes, bn litres

Source: statista

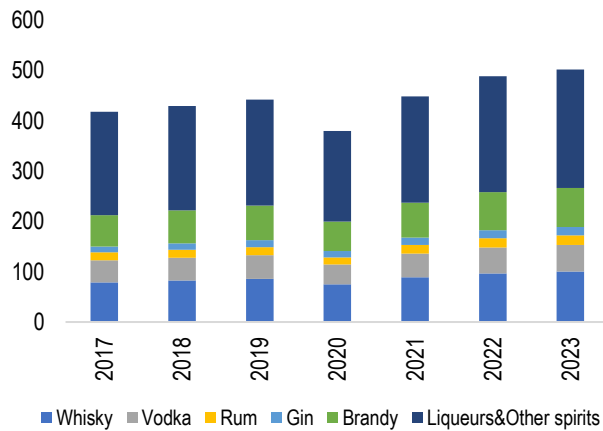
The spirits segment includes distilled alcoholic beverages with an alcoholic content of 20% or over. Its sub-segments include whisky, vodka, rum, gin, brandy, and liqueurs & other spirits. 2019 revenue for the spirits segment of the alcoholic drinks market is estimated at \$443bn, with an estimated CAGR 3.2% p.a. between 2020 and 2023. However, the impact from the coronavirus outbreak negatively affects the market with possible decline between 10% and 25% for FY2019. The average revenue per capita in the segment was \$60.1 in 2019. The average per capita consumption globally is estimated by Statista at 4.4L in 2019. In the spirits segment, the share of out-of-home consumption is estimated at 29% by 2023. The average price per unit in the spirits segment is expected to reach \$13.5 in 2020.

Figure 10. Global Spirits market, \$bn

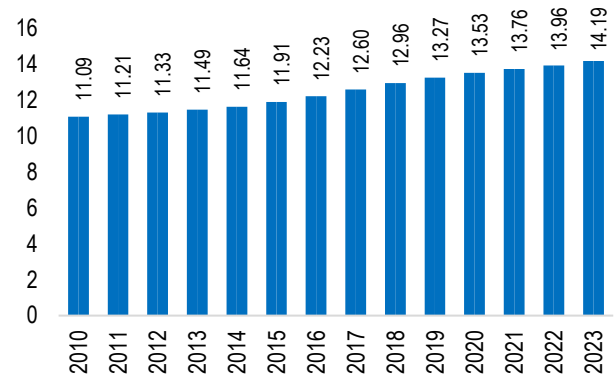
Source: statista, Hypothesis Research

Figure 11. Global Spirits market, bn litres

Source: statista, Hypothesis Research

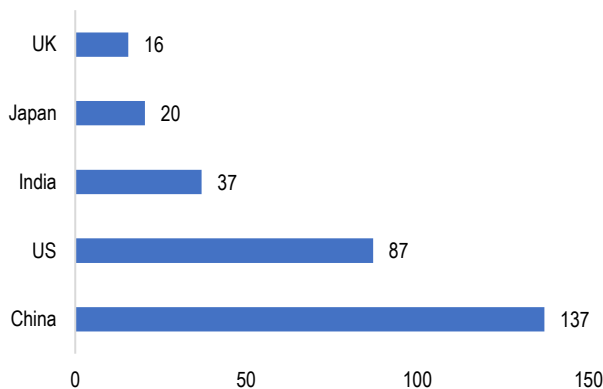
Figure 12. Global spirits market by subsegment, \$bn

Source: statista, Hypothesis Research

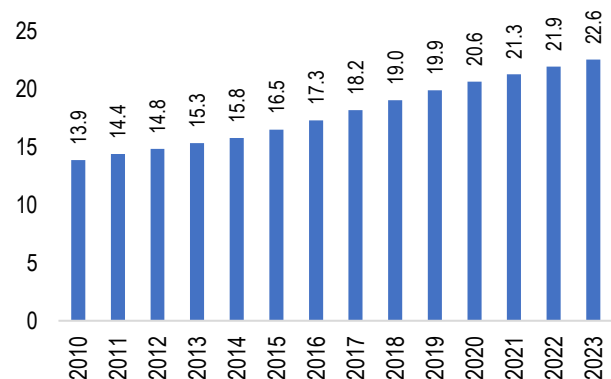
Figure 13. Average price per unit in the Spirits segment, \$

Source: statista

The top five countries by revenue in the spirits segment are China, the US, India, Japan and the UK. Among the largest companies in the global spirits segment are Diageo (UK), Pernod Ricard (France) and Kweichow Moutai (China).

Figure 14. Top-5 countries by revenue in Spirits segment, \$bn

Source: statista

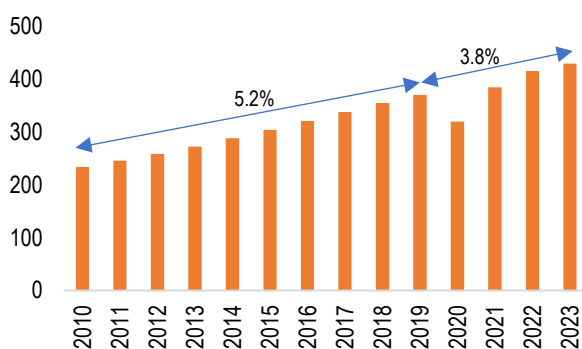
Figure 15. Average price for vodka, \$/litre

Source: statista

The wine market includes beverages derived from fermented grapes. The market includes still wine, sparkling wine (incl. Champagne) and fortified wine. Wine is a mostly agriculturally sourced product and is the smallest segment in the Alcoholic Drinks market. There are several big companies, such as E&J Gallo, Constellation Brands, The Wine Group, Treasury Wine Estate and Vina Concha y Toro, which together control c. 8-9% of the market volumes. The revenue of the segment is estimated at \$370bn in 2019. Most of the revenues are generated in the US. The total volume is expected to reach 27.88bn liters by 2023. The average revenue per capita is estimated at \$49 in 2019, up 3.0% YoY, with average consumption per capita of 3.7L. One liter of wine roughly equals 10 glasses (of 0.1 liters each). A 55% share of the wine segment will be attributable to out-of-home consumption by 2023, according to Statista. The still wine sub-segment, which contains red, white and rose

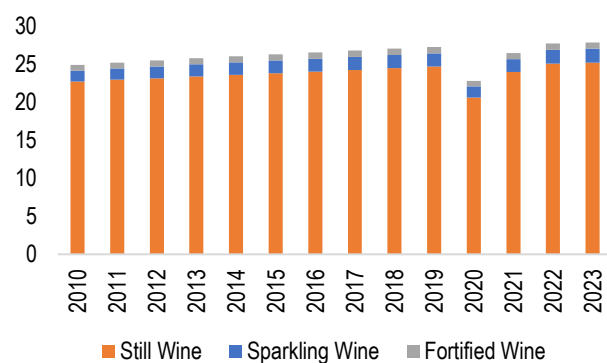
wines without the addition of carbon dioxide or spirit-based alcohol, is growing well globally with an estimated revenue of \$316bn in 2020. The average per capita consumption is 3.2L in 2019. Still wine volume is expected to amount to 25bn liters by 2023. The sparkling wine sub-segment includes wines with the addition of carbon dioxide, such as Champagne, Prosecco or Asti Spumante. Revenues for this sub-segment are estimated at \$41bn in 2019, with sales of 0.2L per capita. The fortified wine sub-segment includes wines which were strengthened with additional alcohol, such as sherry, port wine and madeira. Revenue in this sub-segment is estimated at \$13.4bn in 2019.

Figure 16. Total Wine segment revenues, \$bn



Source: statista, Hypothesis Research

Figure 17. Global Wine segment volumes by sub-segment, bn litres



Source: statista, Hypothesis Research

The cider, perry & rice wine sub-segment includes fermented alcoholic beverages that do not fall into the beer and wine categories, such as fruit wines like cider and perry, rice wines like Sake and Soju, popular in Japan and Korea, and palm wines and similar beverages popular in emerging markets which are cheaper substitutes to beer. The revenue in the segment is estimated at \$128bn in 2019 with most of the revenue generated in Japan, and the average per capita consumption this year is estimated at 6.3L.

Key trends of the global alcohol drinks market

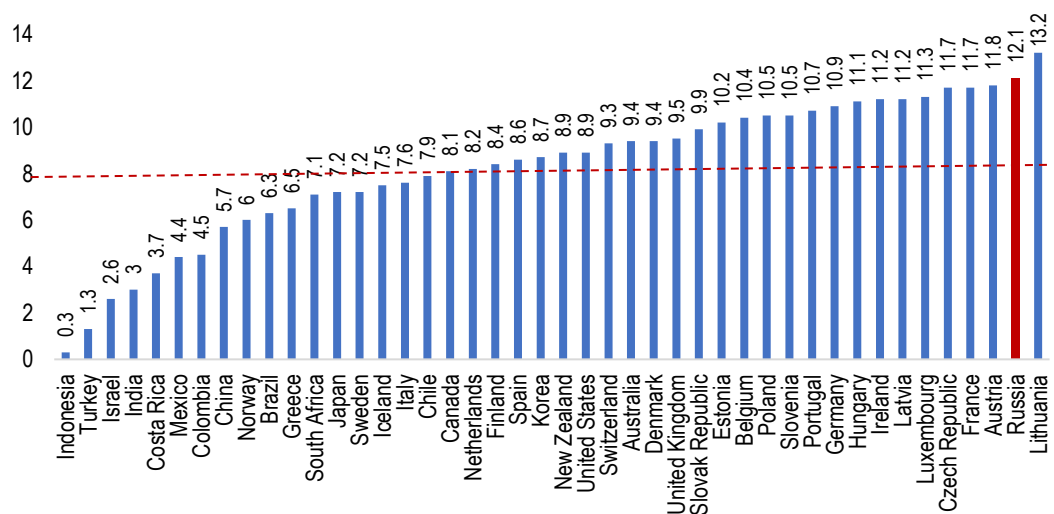
- Population growth and the increasing purchasing power of the population are two general trends supporting the alcoholic drinks market's long-term growth trend.
- Customer's preferences for **healthy lifestyles and wellness** are changing the consumer market for alcoholic drinks in favor of high-quality products.
- **With the trend for premiumization**, consumers are looking for products of superior quality, authenticity and taste.
- Increasing efforts to produce innovative products or '**new editions**' by well-established brands as a way of attracting new consumers and establishing the brand among the younger generation.
- **Purpose driven brands** address the consumer's preference for organic/natural products, specific lifestyle needs, and demographic characteristics etc.
- **Alcohol producers are focusing on sustainability** and promoting responsible drinking that also reflects the brands positioning.

Figure 18. Unstoppable trends in beverages market

Source: Anheuser-Busch InBev

The general trend in the alcoholic drinks market is supportive of the forecast for growing volumes due to increasing population, and greater affordability of alcoholic drinks. However, the structure of the market by segment is changing in favor of wines, reflecting Health and Wellness preferences. The effect on the market of decreasing pure alcohol per capita consumption is by a stronger premiumization trend and greater diversity of tastes in all segments of the alcoholic drinks market.

Alcohol consumption was 8.3L per capita in OECD countries in 2016 with the top of the range taken by Lithuania, Russia, Austria, France, Czech Republic. Historical and cultural traditions of the countries with high alcohol consumption per capita, such as Russia and CIS countries, France, Germany and some others will likely change over time, driven by healthier lifestyles and a shift from drinks with a high alcoholic content to wines and beers.

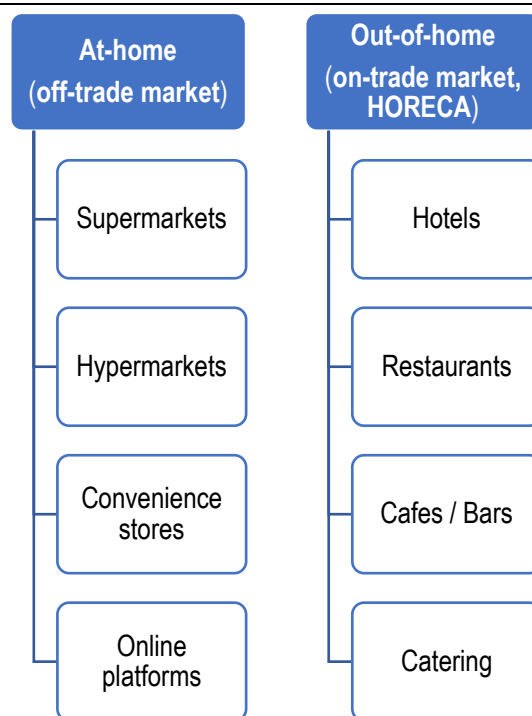
Figure 19. Alcohol consumption total, litres/capita (aged 15 and over), 2016

Source: [OECD](https://data.oecd.org/)

Market structure

The structure of the alcoholic drinks market includes retail sales for at-home consumption and on-premise or foodservice sales for out-of-home consumption. The at-home market, or off-trade market, involves distribution channels such as supermarkets and hypermarkets, convenience stores and similar channels. The out-of-home market also known as the on-trade market, away-from-home market or HORECA includes sales via restaurants, catering services, cafes, bars, hotels and similar establishments. Both at-home and out-of-home markets are valued at the retail price, which include all sales and consumption taxes.

Figure 20. Distribution channels for alcohol drinks market



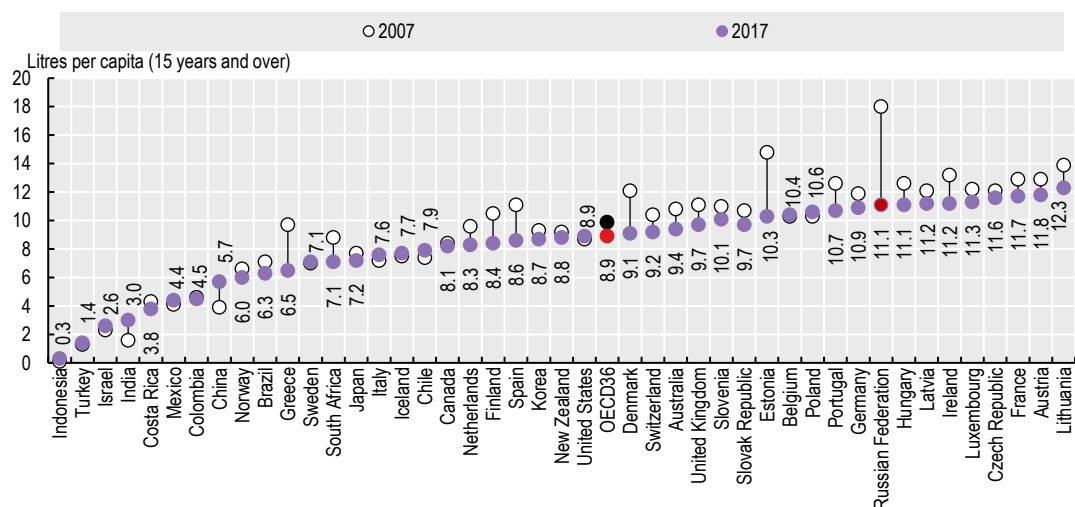
Source: statista

Russian Alcoholic Drinks Market

In Russia, vodka was introduced as an alcoholic drink in the 14th -15th century, probably from Italy. Vodka, according to the current European standard, is made by distilling the liquid from cereal grains or potatoes that have been fermented. In some 'vodka belt' countries, including Russia, Poland, Belarus, Estonia, Finland, Iceland, Lithuania, Latvia, Norway, Sweden and Ukraine, vodka is drunk 'neat' (not mixed with water, ice or other mixers), and often served freezer chilled. In other countries vodka is more popular as an ingredient in cocktails.

The Russian alcohol market is driven by general global trends, including Health and Wellness, Premiumization, and Diversification of the offering/demand for new tastes. The consumption of alcohol by adults has reduced, driven by both better health standards and regulatory changes in the alcoholic market, which have led to the introduction of minimum prices for alcoholic drinks and of taxation for producers. According to OECD, alcohol consumption reduced from 18L per capita (15 years and older) in 2008 to 11.1L per capita in 2017. However, Russia remains among the countries with high alcohol consumption per capita due to its historical tradition, northern location and aging population.

Figure 21. Recorded alcohol consumption among adults, 2007 (Russia-2008) and 2017 (or nearest year)



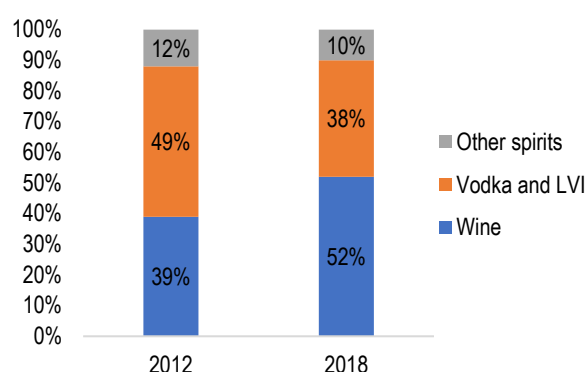
Source: OECD Health Statistics 2019

During the USSR era, the Russian alcoholic beverages market was not well diversified by product, with vodka being the cheapest and dominant product, affordable for most consumers. The efforts of Russian and international alcoholic drinks distributors and producers have been changing the market dynamics and structure, with higher-end products being introduced to Russian consumers since 1990s.

Russia's spirits and wine market

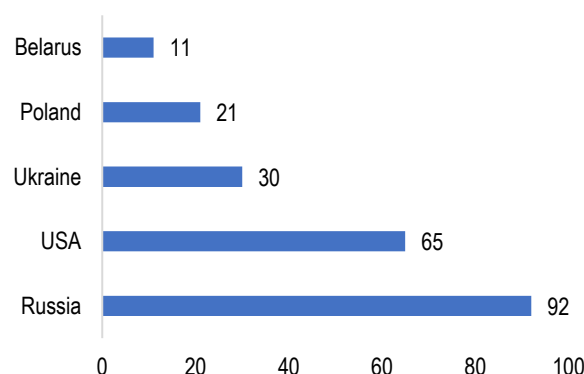
Russia remains among the top-5 countries by vodka consumption, according to IWSR reports, followed by the USA, and three vodka-belt countries Ukraine, Poland and Belarus.

Figure 22. Russian spirits and wine market volume structure in 2012 vs 2018



Source: Rosstat

Figure 23. Top-5 countries by vodka consumption, mn 9L cases



Source: IWSR 2019, All Brands by Volume in 2018

However, Russia's spirits and wine market structure has been changing in favour of wine, driven by consumers' healthier lifestyle choices, higher income per capita and stable economic trends. The share of vodka and liqueurs represented 49% of the Russian spirits and wine market in 2012, but went down to 38% in 2018, according to the Russian State Statistics Committee (Rosstat).

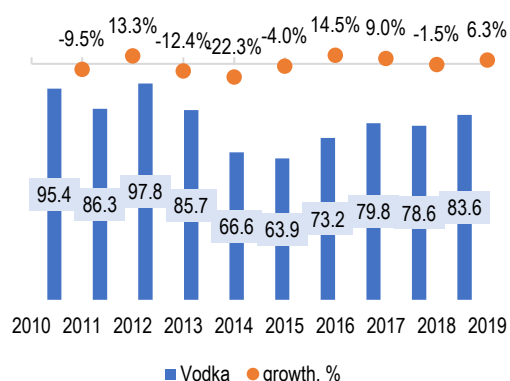
The Russian spirits remains strong during COVID-19 lockdowns. A number of Russian alcoholic drinks producers and distributors recorded an increase in alcoholic drinks sales in March 2020. The limited 'out-of-home' share of alcohol sales in Russia, which accounts several percentages of the largest producers' sales volumes, makes the Russian market less exposed to the negative effects of lockdowns.

Spirits market

Despite the declining vodka consumption trend in Russia, Russian alcoholic drinks producers have maintained relatively stable production of vodka, brandy/cognac and liqueurs. The greater product diversification and the export opportunities played a major role in sales diversification. The total production of spirits and wines in Russia has grown at a 2014-2019 CAGR of 2.3% p.a.

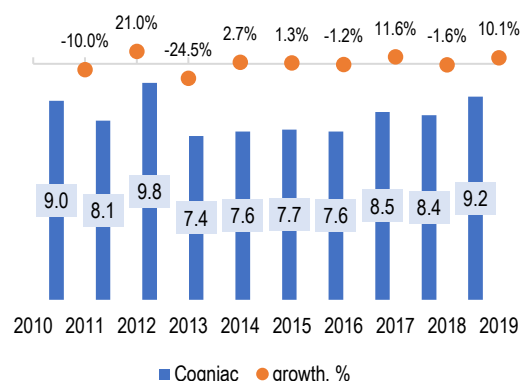
Vodka production bottomed at 64-66mn dal in 2014-2015 due to the grey market expansion in Russia but recovered to 83.6mn dal in 2019. Brandy (often referred as cognac in Russia) reached a low of 7.4mn dal in 2013, recovering to 9.2mn dal in 2019. Russian production of liqueurs with an alcohol content of <25% has been stable for the last three years at 2.7mn dal, while liqueurs at >25% bottomed at 3.9mn dal output in 2015 and recovered to 7.1mn dal in 2019.

Figure 24. Russian production of vodka, mn dal



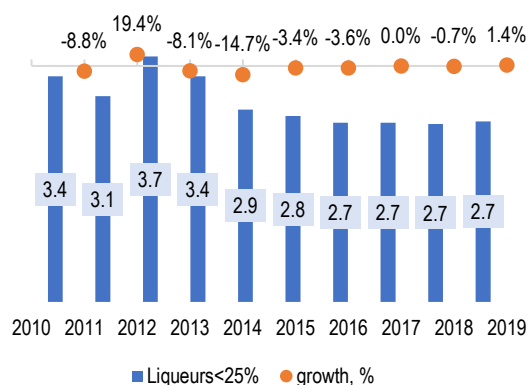
Source: National union of consumer rights protection

Figure 25. Russian production of brandy, mn dal



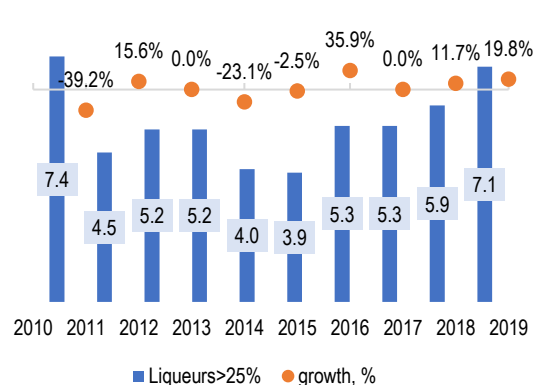
Source: National union of consumer rights protection

Figure 26. Russian production of Liqueurs<25%, mn dal



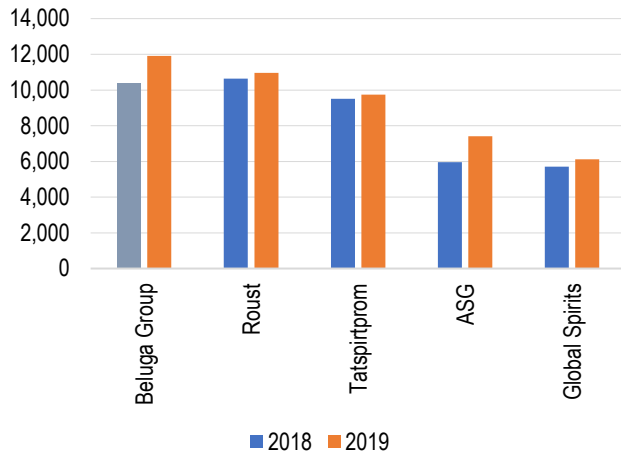
Source: National union of consumer rights protection

Figure 27. Russian production of Liqueurs>25%, mn dal

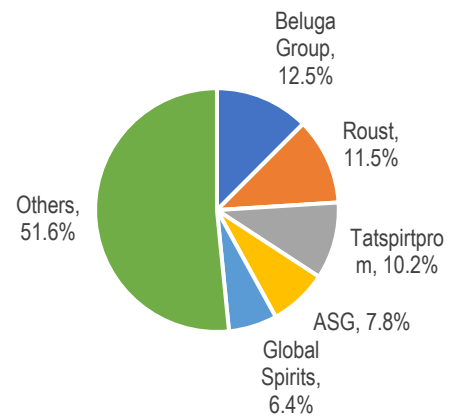


Source: National union of consumer rights protection

Spirits production in Russia is still an unconsolidated industry, with 85% of vodka and liqueurs (LVI – the Russian abbreviation for liqueurs, vodka and other spirits) produced by the top-20 producers. Beluga Group is the largest LVI producer, with a market share of 12.5% in 2019. Roust, ex-Russian Standard group/CEDC, is ranked second in terms of LVI production in Russia with 11.5% and Tatspirom is 3rd with 10.2%.

Figure 28. Top-5 Vodka and LVI producers in Russia, 000 dal, 2019

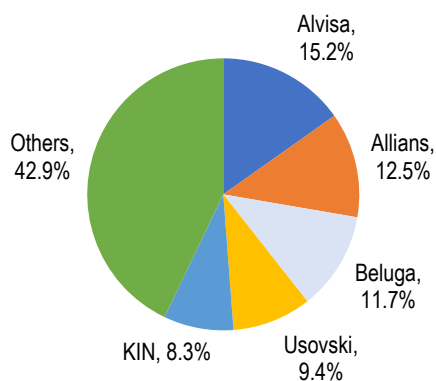
Source: The State Statistics Committee

Figure 29. Market share of top-5 LVI producers, 2019

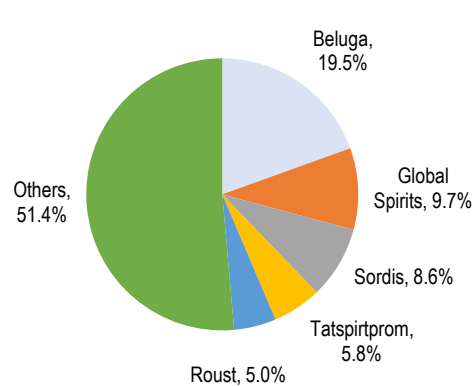
Source: The State Statistics Committee, Hypothesis Research

Overall retail sales of alcoholic drinks in Russia reached 211.5mn dal (excluding beer, cider, poire, and medovukha), up 0.6% YoY.

Beluga Group is ranked number one in the category of liqueurs, vodka and other spirits in Russia with a 12.5% share of total Russian production in 2019. The Group's closest competitor in Russia, Roust Group, produced 10.9mn dal in 2019, up 3.1% YoY. The third-largest spirits company, Tataspirom, produced 9.7mn dal in 2019, up 2.4% YoY.

Figure 30. Top-5 brandy producers, 2019

Source: The State Statistics Committee

Figure 31. Top flavored liquors producers, 2019

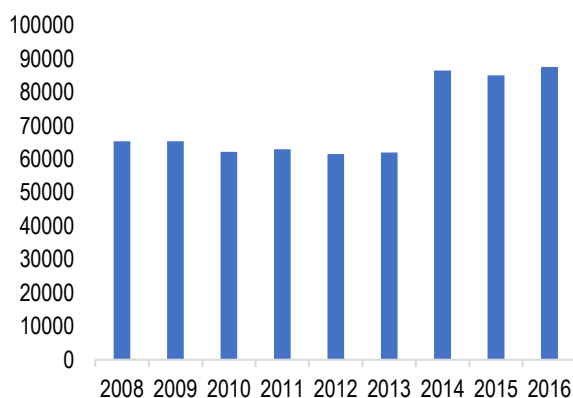
Source: The State Statistics Committee

Russian vodka exporters received some preferential treatment following the changes to the Budget code in 2019. Vodka exports reached \$125mn in 10M2019, up 7.2% YoY. Russian exporters supply vodka to Germany, the UK, Latvia, and some other countries. The potential market for the Russian vodka exports is estimated at \$500mn by 2024, according to REC.

Wine market

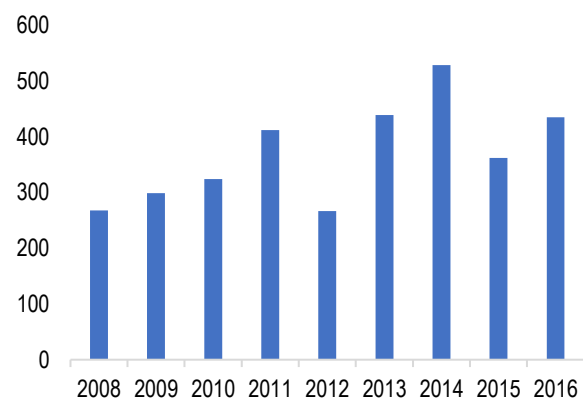
The Russian wine market is a developing segment, covered partially by local producers but mostly by imported brands. According to the Ministry of Industry and Trade, Russia produced almost 940mn bottles of wine and produced 530k tons of grapes (549k tons of grapes is estimated for 2019). The current area of Russia's vineyards is estimated at 95,000 ha, including almost 7,000ha planted in 2018. Russia imported 11.6mn dal of wine materials, mostly from Spain, the Ukraine, Uzbekistan and Uruguay in 2018.

Figure 32. Vineyard surface area in Russia (since 2014, including Crimea), ha



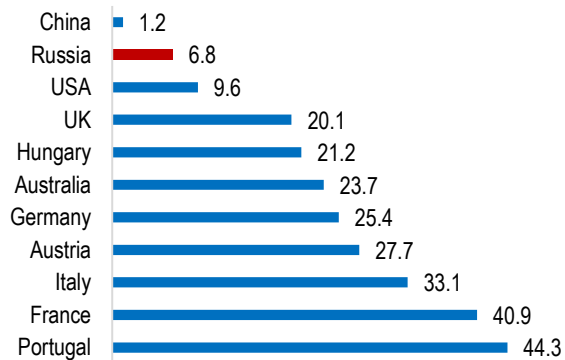
Source: oiv.int

Figure 33. Fresh grapes production, 000t

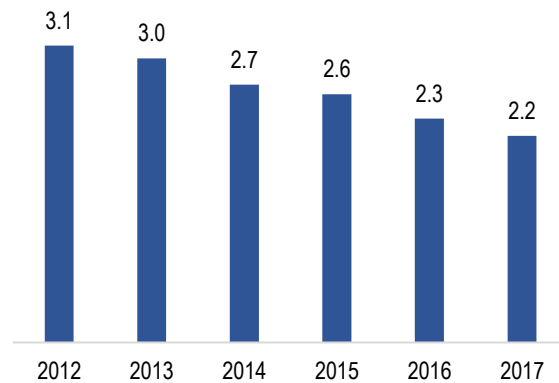


Source: oiv.int

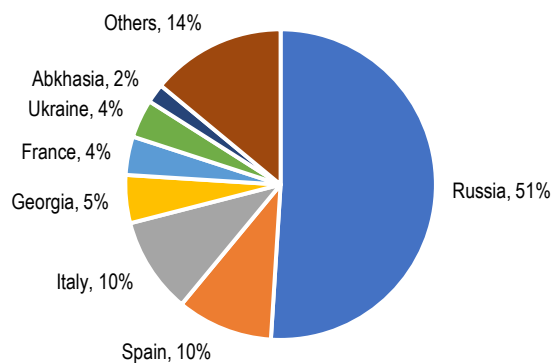
Local wine production is growing now in Russia, with most of the volumes imported. Local producers received tax benefits in 2019, which should provide a stimulus for local grape production and sourcing wine made from local grapes.

Figure 34. Russian average consumption of wine per capita per year, liters

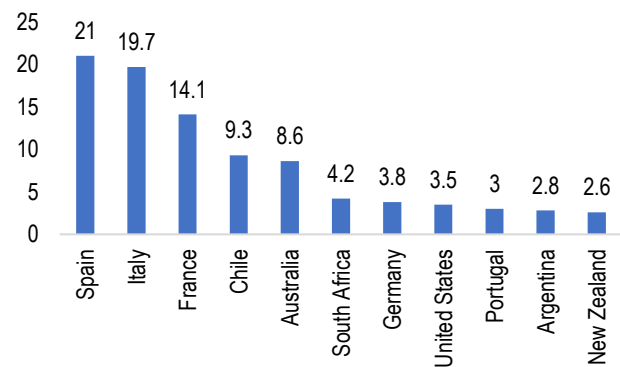
Source: WHO

Figure 35. Average per capita sales of sparkling wines in Russia, litres
<https://realnoevremya.ru/articles/124557-reyting-regionov-potrebleniyu-alkogolya-v-2018-godu>

Domestically produced wine represented over 50% of total Russian wine consumption in 2018. Largest importers of wine to Russia are Spain, Italy, France, and Georgia.

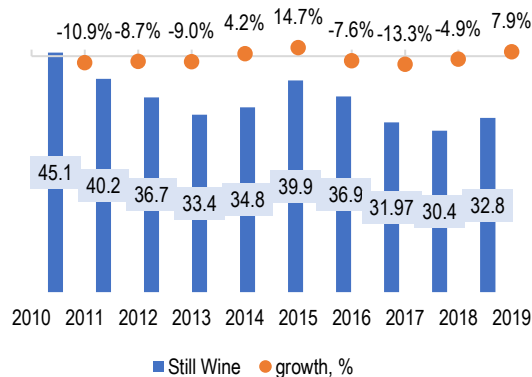
Figure 36. Wine consumption in Russia by country-producer, 2018

Source: FCS

Figure 37. Leading countries in wine export based on volume in 2018, mn hl

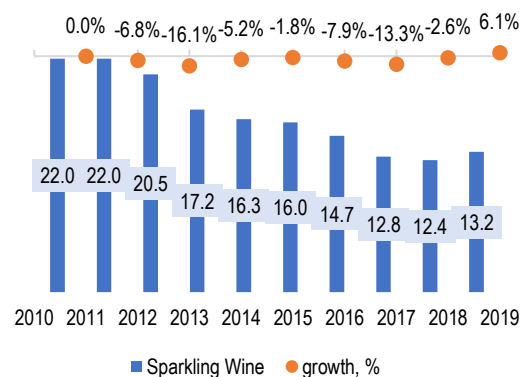
Source: FCS

Figure 38. Russian production of Still Wine, mn dal



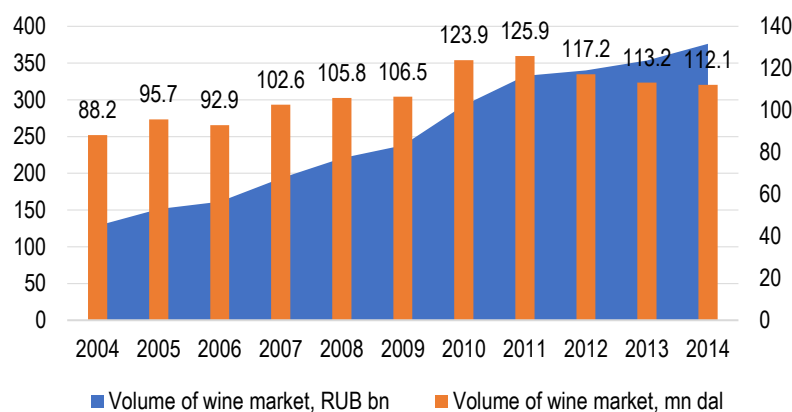
Source: National union of consumer rights protection

Figure 39. Russian production of Sparkling Wine, mn dal



Source: National union of consumer rights protection

Figure 40. Russian Wine market by value (RUB bn) and by volume (mn dal)



Source: Euromonitor International

Russian alcoholic market trends

- **The increasing consumption of wine compared to spirits** due to younger consumers' interest in healthier choices will likely be a long-term trend.
- **Russian spirits production remains stable** due to increasing exports of spirits, increasing diversification of spirits products, and investments in brands by Russian producers, both domestically and internationally.
- **The consumption of vodka has been stable in Russia** for the last four years, while vodka is traditionally consumed 'neat', it may also find an out-of-home consumption market due to increasing popularity of cocktails. Out-of-home consumption of spirits will likely be growing compared to in-home consumption with the increase in personal income. Vodka production has been growing, with 6.9% p.a. CAGR in 2015-2019.
- **Vodka remains the second most popular spirit across the world** after whisky. Russia leads global vodka consumption with 92mn 9L cases compared to 76mn in the USA. That is another driver for Russian companies expanding their exports.

- **Russian vodka exporters receive some preferential treatment** from the government following the changes to the Budget code. Producers of grapes and wine in Russia will also get some tax benefits after the changes to the Tax code in 2019.

Regulation of the alcoholic drinks market

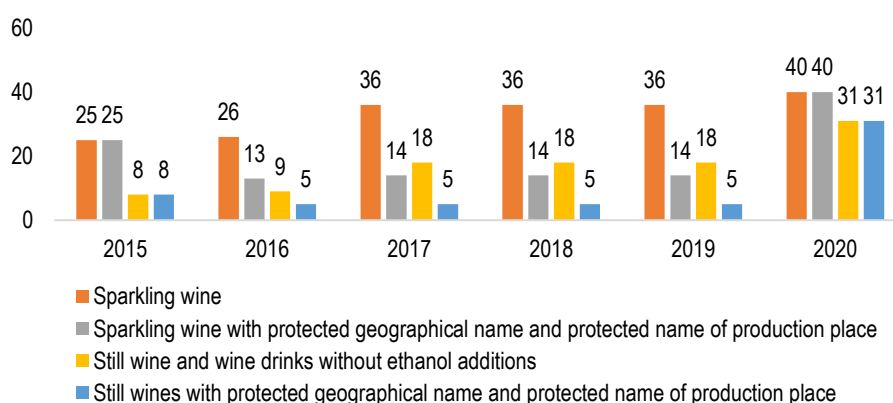
Russian companies have to meet the standards and regulatory requirements of the Russian regulator and any countries to which they export their products.

- **Mandatory marking.** Important changes to the alcoholic drinks market were introduced with the mandatory regulatory requirement for marking of bottles.

All alcoholic drinks, excluding beer, cider, poire and medovukha, have to be marked with a special code if they are produced in Russia and special excise duties code if they are imported into Russia. The mark's code is used by the United State Automated Information System and all participants in the alcoholic drinks market to identify the specific unit of product. The producer or importer of alcoholic drinks is given their code by the authorities after making the required tax or duty payment. The mandatory marking system has improved the position of legal producers, who had previously faced competition from counterfeit or non-legal products imported into Russia from neighbouring countries. According to various estimates, the grey market had had a share of close to 30% of the total alcoholic drinks market. The regulation helped to improve the distribution of products since each bottle carries a unique mark. Consumers of alcoholic drinks are able to check the product using an App as well.

- **Winemaking legislation.** New legislation on wine and winemaking has imposed a restriction on the use of imported wine materials. The law essentially affects the production of sparkling wines, and two large sparkling wine producers Abrau-Durso (accounting for 19% of all imports of wine materials in 2018) and Igristye Wina (25% of all imported materials) which together account for 50% of all sparkling wine output in Russia.
- **Wine excises duties were increased** to RUB31 per litre for still wines and to RUB40 per litres for sparkling wine in 2020. The rate is the same for domestically produced and imported wines, in line with the WTO requirement. A new excise duty for the domestic grapes was also introduced. The excise duty for grapes for the production of wines with a protected geographical name and protected name of production place is set at 30 RUB/ton, and for other wine materials it is 31 RUB/litre. However, producers of wine using the domestic grapes have a tax benefit, so the estimated effect from the increase excise duties may be close to zero for domestically sourced wine, while imported wine may see a price increase of RUB20-40 price per litre.

Figure 41. Wine excises in Russia, RUB/litre



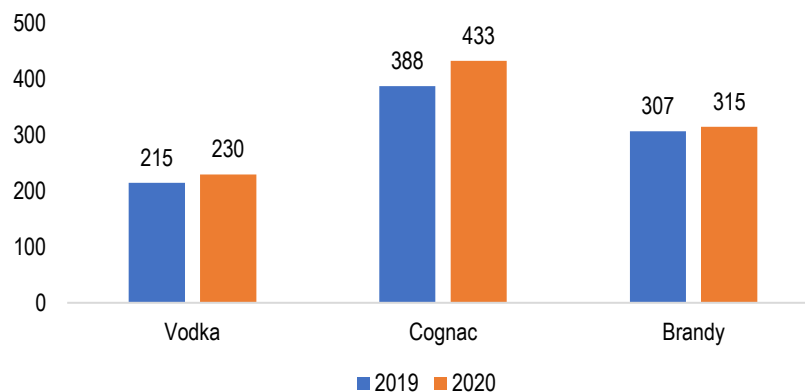
Source: Rosalcoholregulirovanie, Federal custom service, Vedomosti

- **The changes to the Budget code** in Russia lifted the restrictions on government support of alcohol exporters. Now producers and exporters of alcoholic drinks can participate in international exhibitions on preferential terms and recover some licencing expenses. Exporters can also participate in preferential loans programs.

Price environment in Russia

Russia has established a minimum price level for spirits for retail sales. The minimum retail price (MRP) for vodka was set at RUB205 per 0.5 litre in 2018, going up to RUB215 in 2019 and to RUB230 in 2020. Cognac and brandy prices were set at RUB433 and RUB315 per 0.5 litre respectively in 2020.

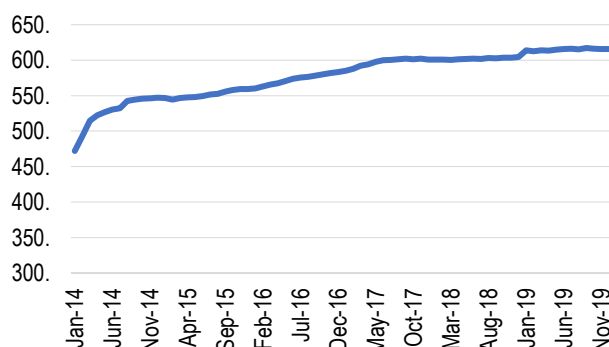
Figure 42. Minimum retail prices for spirits in Russia, RUB per 0.5 litre



Source: The Ministry of Finance

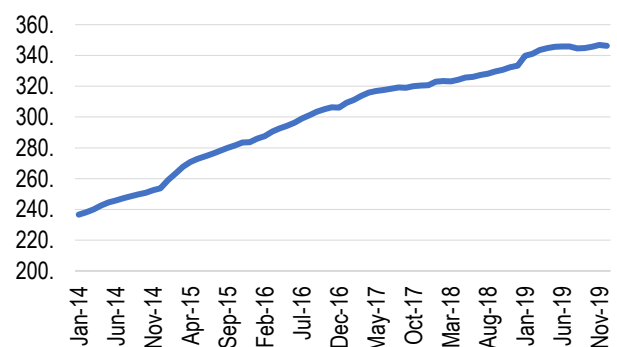
Since the Ruble devaluation in 2014, vodka prices have been growing with a 4.5% 6-year CAGR, while wine prices rose 8% p.a. Domestic prices reflect a still growing market.

Figure 43. Average price of vodka in Russia, RUB/litre



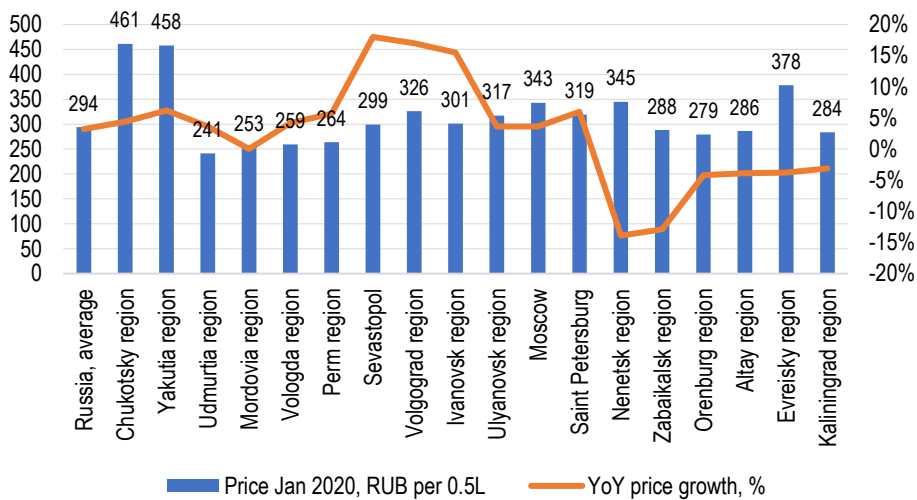
Source: The State Statistics Committee

Figure 44. Average price of sparkling wine in Russia, RUB/litre



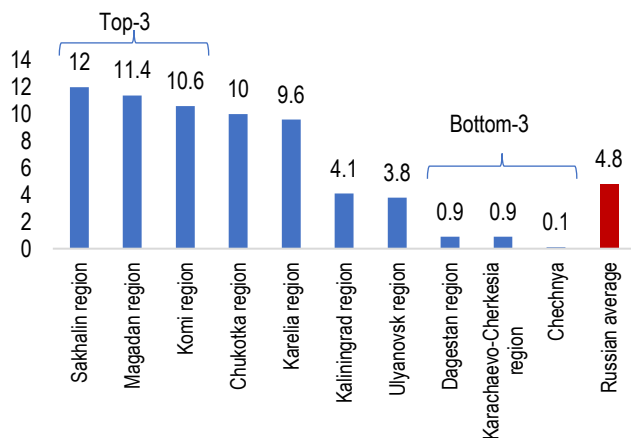
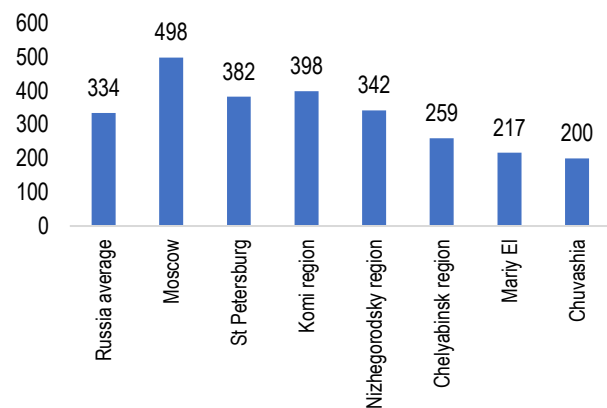
Source: The State Statistics Committee

The average price for vodka varies by region, reflecting the average personal income in the region and local preferences due to weather conditions. The top-5 regions by vodka price include Chukotka, Yakutia, the Evreisky region, the Nenetsky region and Moscow.

Figure 45. Vodka price per 0.5 litre by selected region Jan 2019 - Jan 2020

Source: Evotor

The highest level of vodka consumption per capita is in the Sakhalin, Magadan, Komi, Chukotka and Karelia regions, where the annual consumption exceeds 9L per capita. The average Russian consumption of vodka per capita was 4.8 litres in 2019.

Figure 46. Selected region by vodka consumption per capita, litres**Figure 47. Average check in the alcohol supermarkets Jan'19-Jan'20, RUB by region**

Source: <http://www.cifra.info/>, <https://iz.ru/972635/evgeniia-pertceva/40-gradusov-shiroty-sostavlen-top-5-regionov-liderov-potrebleniiu-vodki>

Source: Ministry of Health of Russia

Key price drivers for the alcoholic drinks market in Russia include:

- The level of minimum retail prices set by the Ministry of Finance.
- Personal income and purchasing power, usually dependant on the region.
- The level of local competition.
- The Russian Ruble exchange rate versus US dollar and Euro which makes spirits and wine imports more or less affordable for domestic consumers.

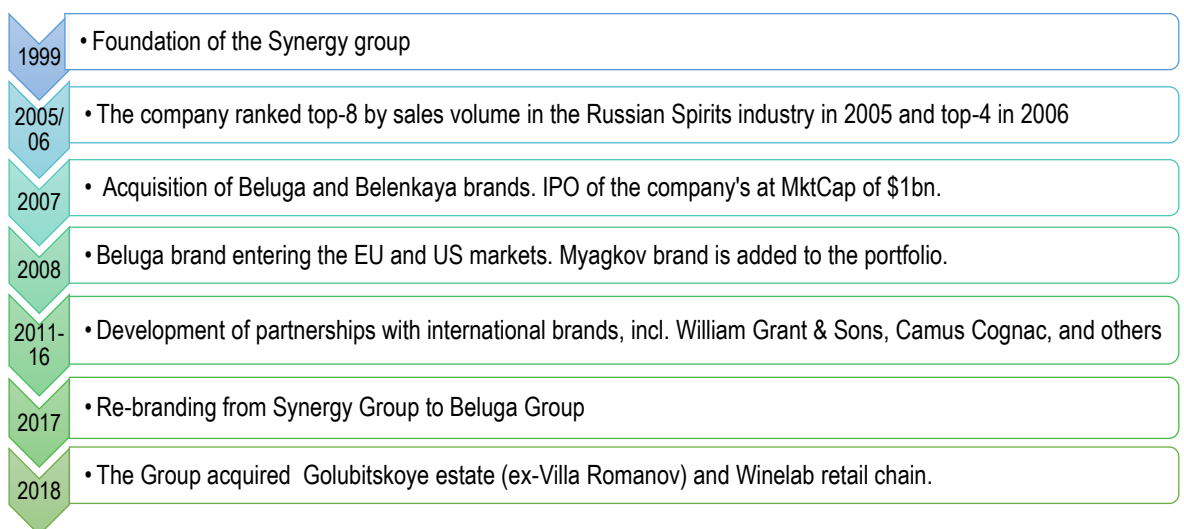
BELUGA Group

Business overview

Beluga Group (MOEX: BELU) is the Russian leading alcoholic drinks company and one of the globally important alcoholic drinks market players. The Group operates a portfolio of spirits and wines brands, benefiting from own alcohol production at its seven production facilities in Russia, an own distribution chain and a fully controlled retail chain Winelab, as well as food production facilities. The Group's vodka brand Beluga is one of the top-five in the global super-premium by sales volumes, while mainstream/sub-premium brands Belenkaya, Myagkov and some other brands have been on the list of best-selling brands globally for the last five years. In 2019, Beluga Group started production of own wine at the Golubitskoye estate, one of the few premium-wine estates in Russia. The Group's diversified portfolio of own and partner brands allow it to maintain a sustainable growth of sales volume and to invest in innovation of its own brands.

The Group was founded in 1999 as Synergy Group. In 2002, the company acquired its first distillery enterprise, the Ussuriysky Balsam Plant, and added five more plants to its production facilities over the next five years. This allowed the company to become one of the largest players in the Russian spirits market by 2007, when Beluga and Belenkaya brands were acquired to build an own brand portfolio. Synergy Group became public in 2007, achieving a \$1bn valuation during its IPO. In 2008, the company launched the Beluga brand in Europe and the US, and added the Myagkov brand to its portfolio. In 2010, the Group reached production volume of over 140mn liters of beverages. In 2011, it signed an executive agreement with William Grant & Sons and Camus Cognac House for the distribution of their products in Russia. In 2013, the Group launched its own whisky Fox & Dogs, brandies Bastion and Le Lion de Pierre, and liqueur Doctor August in Russia. At the same time the Beluga brand entered the Chinese market. The Group expanded its imported brands portfolio in 2014-2020, adding to the portfolio such well-known names as Torres brandy and wines, Barcelo rum, Noy Armenian brandy, Cono Sur, Mazi wines. Since 2010, Beluga Group is the leader of the Russian market in the vodka and whisky segments, and alcoholic beverages. In 2017, the Group also rebranded, changing its name from Synergy Group to Beluga Group, reflecting the strong Beluga brand recognition.

Figure 48. Beluga Group history



Source: Company data

Diversification followed with the acquisition of the retail chain Winelab, which was expanded to 604 stores by the end of 2019. Geographically, the Group operates across Russia from

Moscow and Saint Petersburg to Vladivostok, with its retail chain present in three main regions, including St Petersburg and North West (64), Moscow and Moscow region (171), Far East (336).

Figure 49. Beluga Group Winelab retail chain major presence



Source: Company data

In addition to spirits production and distribution, Beluga Group has entered an agriculture segment with the acquisition of the Golubitskoye estate in the Taman region. In 2019, the Golubitskoye vineyard produced 2,388 tonnes of grapes, which translates to approximately 2mn of bottles of wine, half of which will be sparkling wines, to be offered to consumers in 2020.

The Golubitskoye estate was founded in 2007 as Villa Romanov on a 231 ha area near Temryuk town on Tamagne-Golubitskaya Strelka spit between the Azov sea and Akhtanizov Liman in the Krasnodar region. The vineyards were planted in 2009-2013 and the first grapes were produced in 2016. There are seven international grapes varieties grown on the estate: white varieties include Sauvignon blanc, Riesling, Chardonnay, Pinot Gris; and red variety including Merlot, Pinot Noir and Cabernet Sauvignon. The Golubitskoye estate produces wines with a protected geographical indication (ZSU) "Kuban. Taman peninsula." The annual capacity of the vineyard is 2mn bottles, but Beluga Group aims to expand capacity to 10mn bottles on a 5-7 years horizon.

Figure 50. Golubitskoye estate in Krasnodar region



Figure 51. Golubitskoye estate - vineyard



Figure 52. Golubitskoye estate – wine facilities

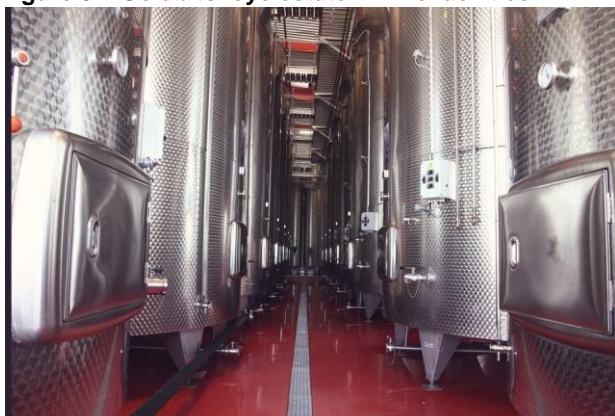


Figure 53. Golubitskoye estate – production facilities

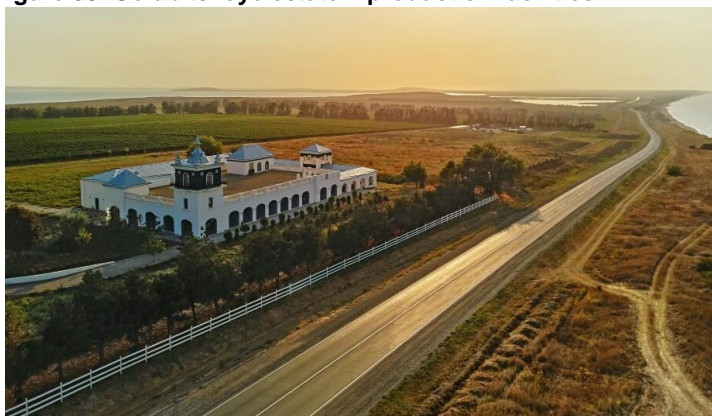


Figure 54. Golubitskoye estate – storage facilities

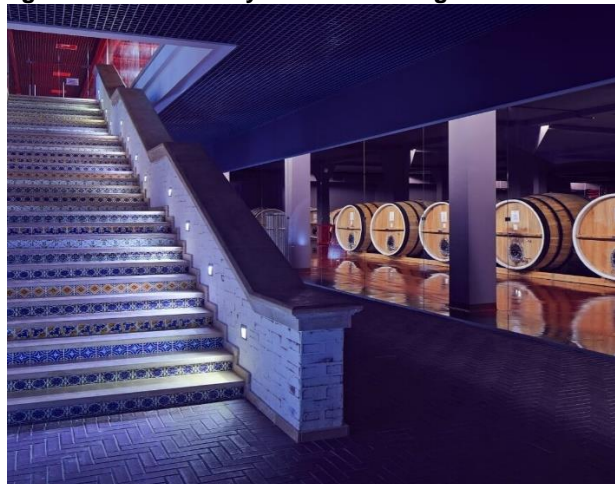
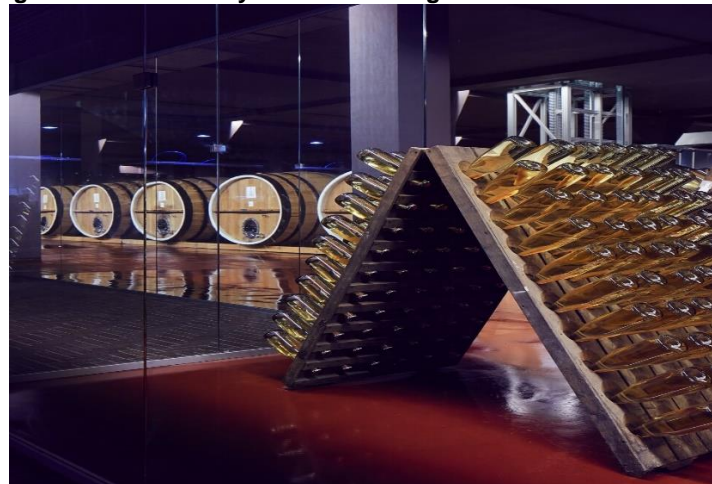
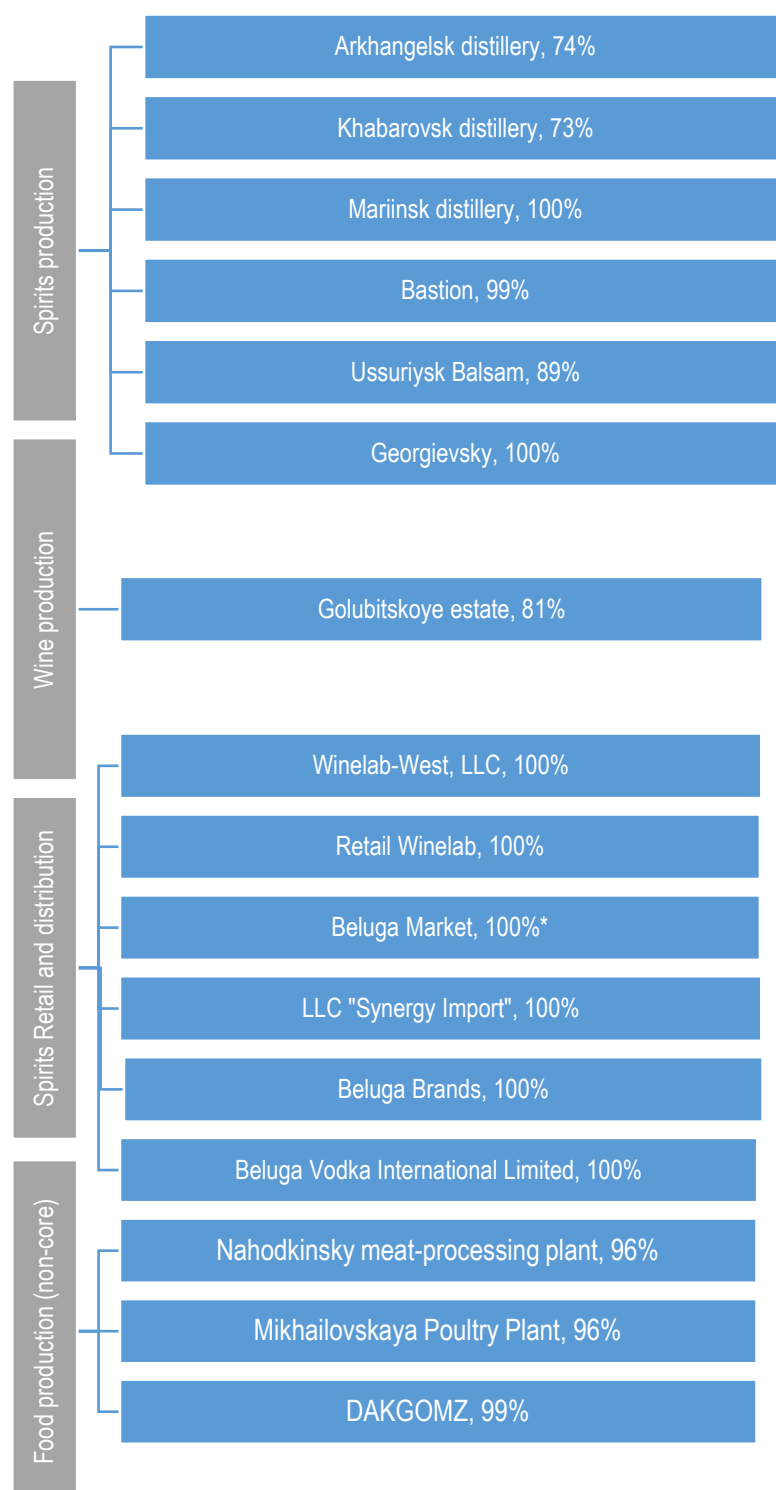


Figure 55. Golubitskoye estate – storage facilities



Source: company

Figure 56. Beluga Group corporate structure as of end 2020 (voting share as of 31/12/2019)

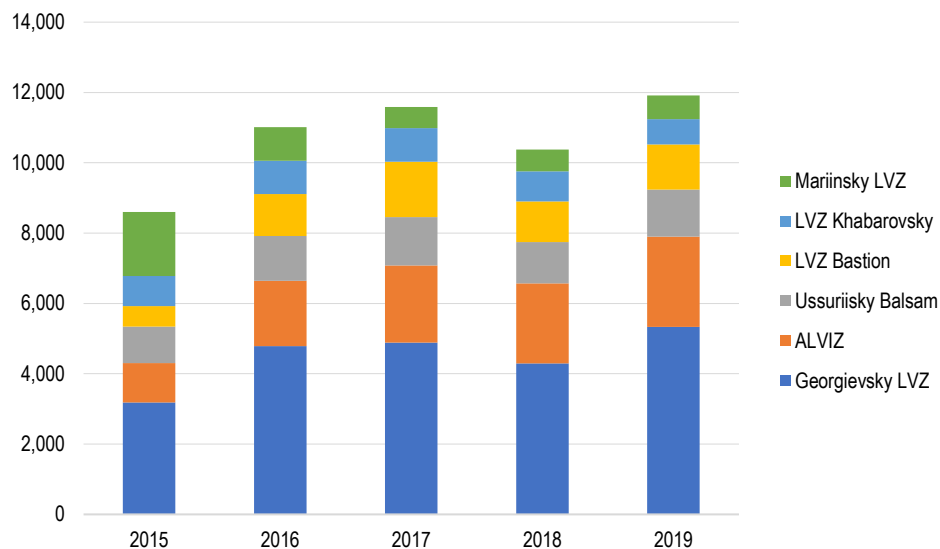


Source: Company data, *) also includes 100% share in the marketing companies Beluga Market Khabarovsk, Beluga Market Arkhangelsk, Beluga Market Vostok, Beluga Market Far East, Beluga Market Region, Beluga Market Vladivostok, Beluga Market Perm, Beluga Market West.

Production

Beluga Group operates six distillery facilities across Russia in the Arkhangelsk region, Moscow region, Primorskiy region, Khabarovskiy region, Kemerovo region and Perm region and one vineyard in Krasnodarskiy region. The annual production of spirits reached 12.98mn dal in 2019, up 14% YoY. Own distribution and product diversification contributes to the company's sustainable production growth despite volatile trends in the Russian spirits market.

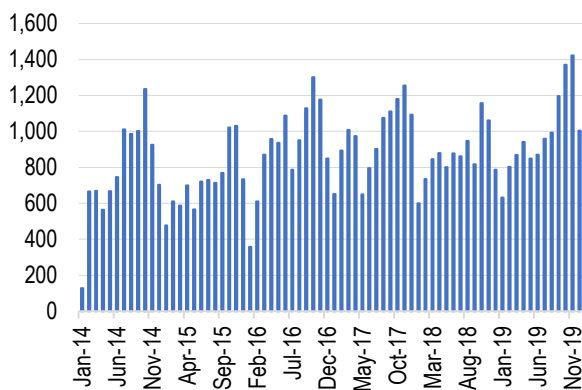
Figure 57. Beluga Group production dynamics by plant, 000 dal



Source: The State Statistics Committee

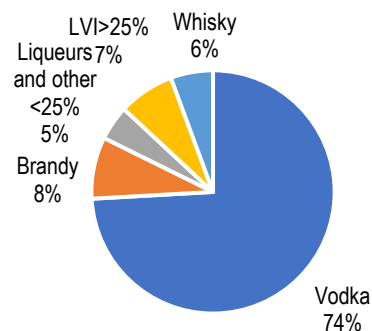
Spirits production is seasonal, with the peak in October-December due to a winter holiday season starting in December and lasting until mid-January in Russia. January-February production is usually weaker.

Figure 58. Beluga Group monthly production volumes, 000 dal

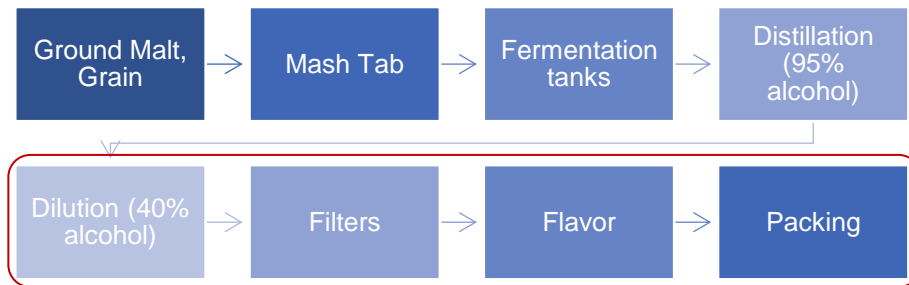


Source: The State Statistics Committee

Figure 59. Beluga Group Spirits production structure, 2019



Source: company data

Figure 60. Vodka production chart and Beluga Group business processes (red circle)

Source: Hypothesis Research

Beluga vodka is produced by the Mariinsk distillery in Siberia. There are six SKUs of Beluga vodka: Noble, Transatlantic, Allure, Goldline, Celebration, and Beluga Epicure by Lalique. Vodka production process includes several stages. Beluga family also includes two bitters: Beluga Hunting berries and Beluga Hunting herbal. The essential component of the vodka formula is water, which is sourced from an artesian well around 200m underground. Another component is a wheat malt spirit. The filtration process includes a triple filtration through charcoal, impregnated silver and sand (or quadruple for the Transatlantic flavor, with the addition of cotton). The final stage includes maturation for one month for Noble, 45 days for Transatlantic, 2 months for Allure, and 3 months for Gold line. The international footprint of the Group includes the office and dedicated team in the USA and the ambassadors in Germany, France, the UK, Georgia, Kazakhstan and the Baltic states.

Figure 61. Beluga vodka flavors

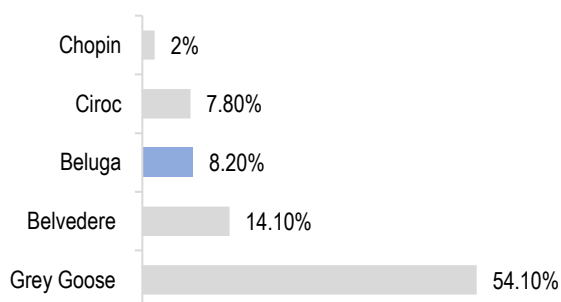
			
Flavor	Noble	Transatlantic	Allure
Filtration	Triple	Quadruple	Triple
Maturation	1 month	45 days	2 months
			
Flavor	Gold Line	Celebration	Epicure
Filtration	Triple	Triple	Triple
Maturation	3 months	3 months	3 months

Source: company data

Brands

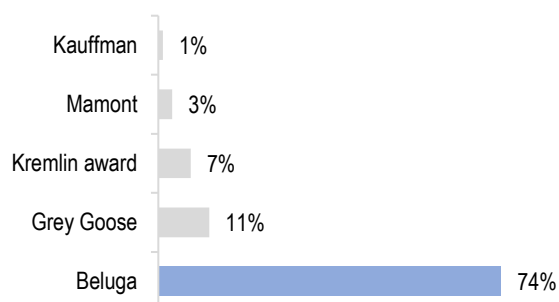
Beluga Group has a brand portfolio, which includes own brands and imported or partners brands. The Group manages 11 vodka brands. Since 2007, when two major brands Beluga and Belenkaya were added to the company's brand portfolio, the company has been a participant in the international influential ratings survey held annually by Impact, Drinks International Millionaires Club, IWSR, The Spirits Business.

Figure 62. Top-5 super-premium vodka brands globally



Source: Source: IWSR (2018), IWSR traditional vodka (2018)

Figure 63. Market shares of top-5 super-premium vodka brands in Russia



Source: Source: IWSR (2018), IWSR traditional vodka (2018)

Figure 64. Beluga Group own brands

Segment	Vodka	Brandy	Wine	Liqueurs/Other
Super premium	 Beluga vodka	 Bastion, Beluga Hunting	 Golubitskoe estate	 Green Baboon
Sub premium / Premium	 Myagkov, Arkhangelskaya, Snow Owl, Copper Horse, Veda	 Tiflis Treasure, Trouble Maker, Le Lion de Pierre, Eagle's Rock	 Vogue	 Arkhangelskaya, Myagkov
Middle	 Belenkaya, Russian Ice	 Zolotoy Reserve, Staraya Gvardiya, Fox & Dogs	 Tiflis Treasure	 Trinity, Ussuriysky, Doctor August, Captain's rum
Mainstream	 Georgievskaya, Tsar	 Ardeli, Georgievskaya	 Arbatskoye	

Source: Company data

Figure 65. Beluga Group selected imported brands**Super premium****Sub-premium / Premium****Middle**

Source: company data

Beluga vodka brand holds one of the leading positions in the international global vodka ratings, competing with global producers in terms of global distribution. Beluga vodka is an important brand with global recognition. The brand's sales volumes have been increasing for several years, including volumes delivered to the USA, Israel, Europe and the CIS. The company is developing the brand sales via international airports through Duty Free operators. Global Travel Retail is an essential distribution channel for Beluga vodka. The Group also exports other vodka brands Belenkaya, Myagkov and Russkiy Led presented in this channel.

Figure 66. 2020 Brands report – Top trending brands

	Brand	Owner	Logo
1	Ketel One	Diageo	
2	Grey Goose	Bacardi	
3	Tito's	Fifth Generation	
4	Absolut	Pernod Ricard	
5	Beluga	Beluga Group	
6	Haku	House of Santory	
7	Belvedere	LVMH	
8	Nikka Coffeey	Nikka Whisky	
9	Reyka	William Grant & Sons	
10	Stolichnaya	SPI Group	

Source: <http://edition.pagesuite.com/html5/reader/production/default.aspx?pubname=&edid=929b08c3-9ea0-41d6-896d-25f15ec9d463>

Strategy

Beluga Group is one of key players in the Russian alcoholic drinks market, leading on market share in the spirits segment, and an important player in the global alcoholic drinks market. The Group developed a portfolio of own brands and promotes partners' brands in Russia, with partners including important producers such as William Grant and Sons, William Lawson's, Camus, Masi Agricola, Frescobaldi Group, Torres, Domaines Barons de Rothchild, Noy, and Barcelo.

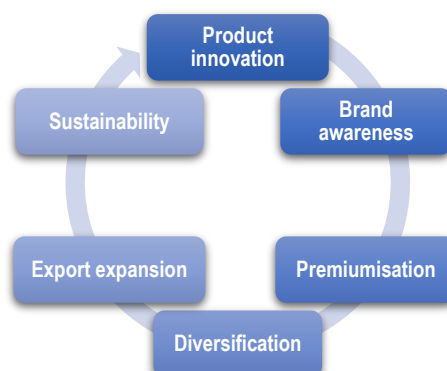
Key strategy priorities:

- Diversification of product range in Spirits and efficient development of own and partners' brands in Russia.
- Higher diversification in the wine segment, including focus on production of own premium still and sparkling wines.
- Focus on production and promotion of high-quality premium products.
- Innovation and product development.
- Investments in brand awareness.
- Enhancement of Beluga distribution platform in Russia and abroad.
- Further development of distribution platform.
- Exports expansion and promotion of Beluga brand abroad, including through Global Travel Retail.

The Group's key targets include the following Sustainability elements:

- Maintaining the highest sustainability standards.
- Driving productivity while keeping costs low.
- Providing the highest-quality products to consumers.
- Promoting responsible drinking.
- Reducing environmental impact.
- Building healthy and thriving communities.
- Having high standards of governance and ethics.

The Group's market position is associated with premium products and high product quality. Product range diversification and investment in innovation are two long-term growth factors helping the Group to maintain the long-term growth.






Marketing initiatives

The Group's main marketing efforts are focused on trade marketing activities aiming to increase sell-out from the shelves. The activities include "Golden shelf" product placing, additional point-of-sales in stores, discount policy and others.

The Group's latest marketing activities of Beluga vodka are focused on annual events and regional campaigns which contribute to brand recognition. Beluga, as a global brand receives the essential marketing support, including Global Travel Retail marketing.

Figure 67. Selected marketing initiatives by brand in 2020

Global brands	Local brands	Wines
Beluga	Myagkov Organic	Golubitskoye brand
		

Source: company data

Operational performance

For the Alcohol segment, we note that in 2020 the spirits market in Russia is still performing well with sales volumes increasing across the spirits and wine segment in 1Q20. Beluga Group reported strong 1Q20 operating results. The sales volumes rose by 19% YoY to 3,201k 9L cases, driven by the company's own brands sales growth by 17% YoY and 40% YoY increased of importer brands sales. The sales increase was due to higher sales volumes of Belenkaya and Arkhangelskaya Severnaya Vyderzhka in the vodka category; Zolotoy Reserve in the brandy category, Fox& Dogs in the whiskey category, and Green Baboon in gin.

However, several challenges may affect the operating performance of the players in the spirits segment in 2020.

- The impact of coronavirus (COVID-19) on global travel and the Global Travel Retail performance. The travel restrictions have affected the Global Travel Retail segment, with an expected sale decline in 1H2020 due to the spread of COVID-19 and the cancellation of flights.

- The Ruble devaluation following the sharp oil price correction will likely affect prices of imported products in Russia making them less affordable for domestic customers. Import volumes may be affected as a result.
- The pricing environment in Russia may change following the Ruble devaluation and fall in the oil price.

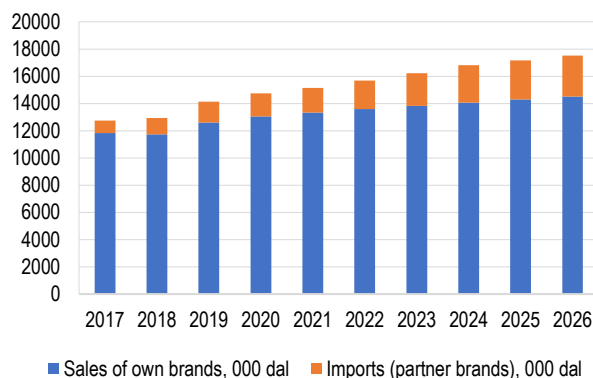
The company has enough capacity to increase production to total 15mn dal per year at its six spirits production plants.

There are several major drivers for the company's sales and revenue growth:

- Diversification, including expansion of imported partner's brands in Russia.
- Premiumisation of sales mixed.
- Beluga vodka brand development and increase in exports.
- Own premium wine production growth.

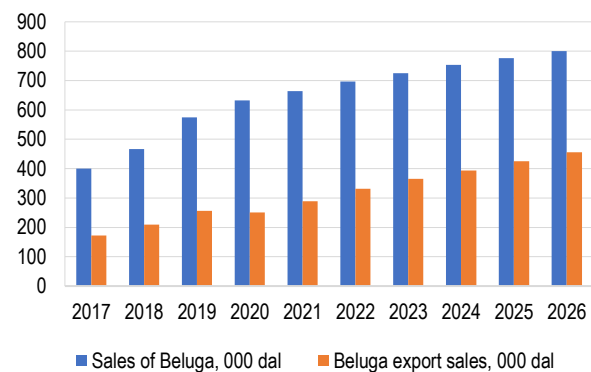
We expect Beluga's volumes will grow at a 4.8% CAGR, most of that growth in the next 2-3 years.

Figure 68. Beluga Group sales of own and imported brands, 000 dal



Source: company data, Hypothesis Research

Figure 69. Beluga vodka production and exports, 000 dal

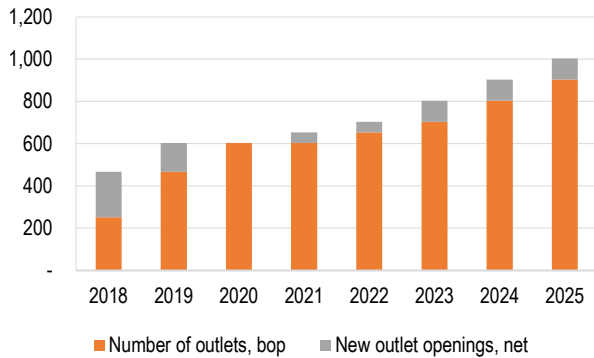


Source: company data, Hypothesis Research

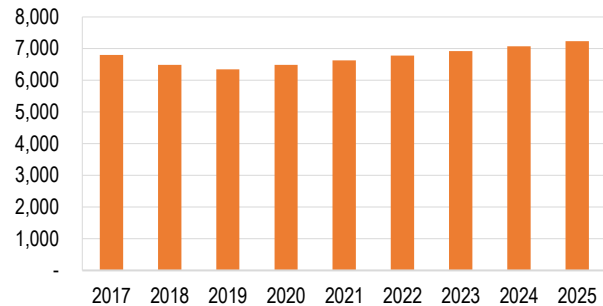
We consider that assuming growth of the Beluga price to be in line with CPI as a conservative approach. However, we set apply a at 2.9% CAGR for the forecasting period. The CPI was at 3% in December 2019, 2.4% in January and 2.3% in February 2020, but the ruble devaluation may drive the inflation up. We make a conservative assumption of 3% for imports price growth, while assuming a higher growth rate if the ruble exchange rate stays above RUB70 through 2020.

In the Retail segment, we assume the Group expands the Winelab retail chain by 400 stores between 2021 and 2025 from 604 stores at end-2019. The Retail segment should pick up in 2020-2021 due to a sales increase in recently opened stores. The further expansion of own and imported brand sales should support the company's growth in this segment.

The Food segment is a mature business for the Group, and also considered non-core. The revenue in this segment is expected to be stable.

Figure 70. Retail segment: outlet number, units

Source: company data, Hypothesis Research

Figure 71. Beluga Group Food segment revenue, RUB mn

Source: company data, Hypothesis Research

Financial forecast

Our financial forecast for Beluga Group is based on the macroeconomic assumptions we present below. However, the effect of the Ruble devaluation and oil price drop is hard to estimate in the short term. We expect Brent oil prices at \$25-45/bbl in 2020-2021. That will likely mean an exchange rate for the Russian Ruble at 69-78 RUB/USD. We also expect some modest acceleration of inflation from below 3% annual estimate to an average 3.5-3.8% p.a. for 2020-2023.

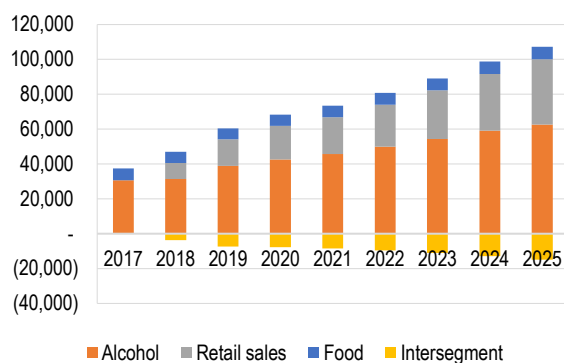
Figure 72. Macro forecast for the Russian economy

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Real GDP growth	-0.2%	1.5%	2.3%	1.3%	1.5%	2.0%	2.5%	2.5%	2.5%	2.5%
Industrial Production Growth	1.1%	1.0%	2.9%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%
Oil price, Brent	43.6	54.3	71.1	69.0	35.0	45.0	56.3	55.0	53.5	60.0
USD/RUB at the end of year	60.7	57.6	69.5	61.9	69.0	70.0	70.0	70.0	70.0	70.0
USD/RUB average	67.0	58.4	62.7	64.6	72.0	72.0	70.0	70.0	70.0	70.0
CPI, eop Dec-Dec	7.1%	3.7%	4.3%	3.0%	3.8%	3.8%	3.5%	3.5%	3.0%	3.0%

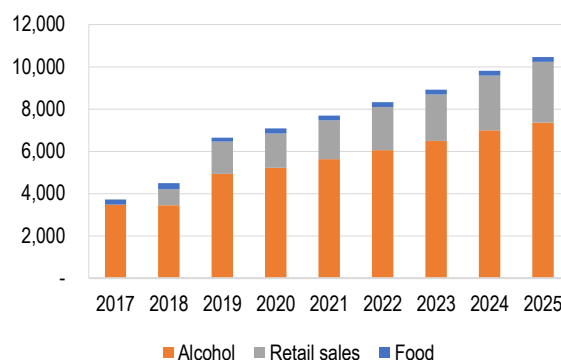
Source: gks.ru, Hypothesis Research estimates

Revenue structure

Our revenue forecast for Beluga Group is based on our forecasts for the company's three segments: Alcohol, Retail, and Food. The company has a relatively stable and mature Food segment, which mostly services the Far East region and some Central Russia regions. Revenue for the retail segment was first reported in 2018, after the acquisition of a controlling stake in the Winelab alcohol retail chain. The Group invested in the specialised retail chain during 2018-2019 and reported 604 stores open at the end of 2019, compared to 252 stores at the end of 2017 and 468 stores at the end of 2018. The Group plans a further modest expansion of the retail chain by 50 stores per year in 2021 and 2022 and by 100 stores a year in 2023 and 2024 stores. The Group expects an operating margin improvement in the Retail segment as newly opened stores will ramp-up sales and revenue per store.

Figure 73. Beluga Group revenue by segment, RUB mn

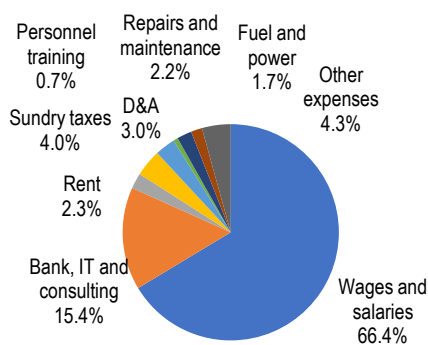
Source: company data, Hypothesis Research

Figure 74. Beluga Group EBITDA by segment, RUB mn

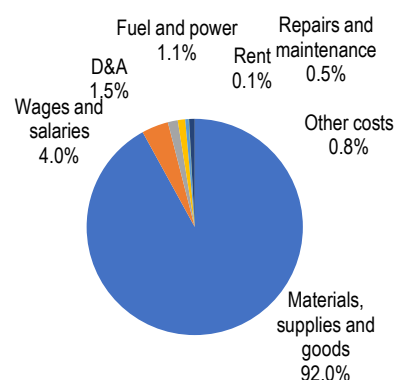
Source: company data, Hypothesis Research

Cost structure

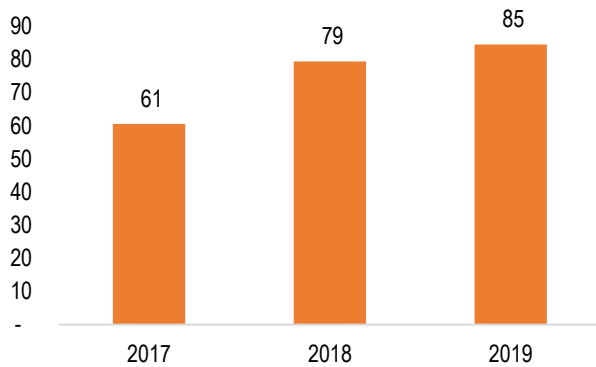
Beluga Group cost structure is relatively stable with materials, supplies and goods making up a 92% of total CoGS, and wages and salaries accounting for over 60% of general and administrative expenses. Distribution expenses is another large category representing an over 21% share of the Group's revenue.

Figure 75. Beluga Group general and administrative expenses structure in 2019

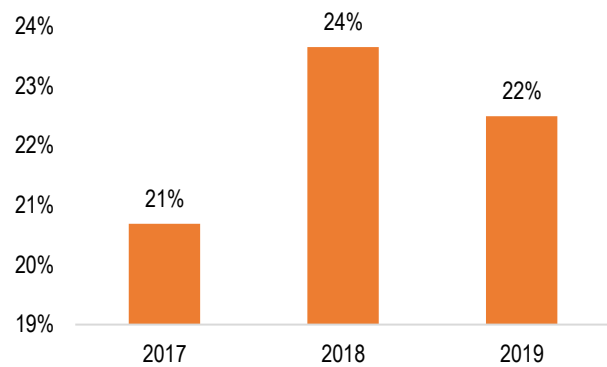
Source: Company data

Figure 76. Beluga Group cost of sales structure in 2019

Source: Company data

Figure 77. Group's distribution expenses per litre, RUB

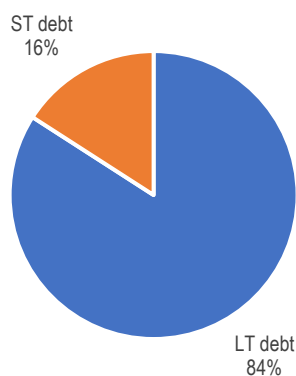
Source: Company data, Hypothesis Research

Figure 78. Group's distribution expenses/revenue

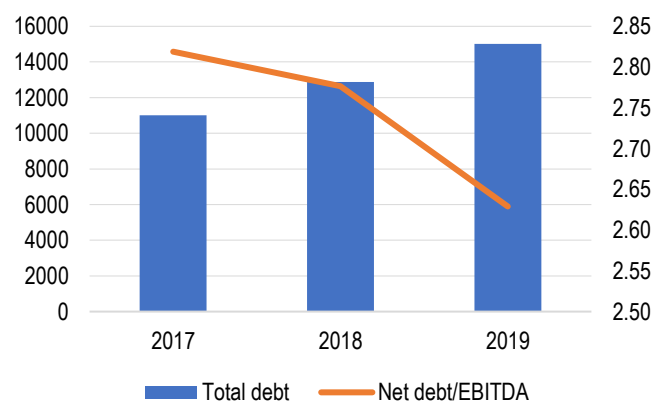
Source: Company data, Hypothesis Research

Debt structure

Beluga Group has followed a conservative capital structure policy, keeping net debt/EBITDA below 2.7x. The company has several bonds issued and three of them are currency traded on Moscow Exchange with a 6.9-9.8% yield as of 8 April 2020. The Group has received the long-term rating of the issuer's default in foreign currency at B+, Stable from Fitch Ratings in February 2018, and ruA- from Expert RA in December 2019. The Group placed two RUB5bn bond issues in 2019, both for 3.5 years to extend the debt maturing in 2020.

Figure 79. Beluga Group debt structure as of 31/12/19, %

Source: Company data

Figure 80. Beluga Group debt dynamics and Net debt/EBITDA*

Source: Company data, Hypothesis Research, *) Based on EBITDA before IFRS 16

Figure 81. Beluga Group profit and loss statement, RUB mn

RUB mn	2017	2018	2019	2020	2021	2022	2023	2024	2025
Revenue	37,303	43,411	53,074	60,528	64,992	71,063	78,021	85,804	92,452
Cost of sales	23,628	26,521	33,547	39,425	42,041	45,832	50,301	55,189	59,456
Gross profit	13,675	16,890	19,527	21,103	22,952	25,231	27,720	30,615	32,996
Gross margin	36.7%	38.9%	36.8%	34.9%	35.3%	35.5%	35.5%	35.7%	35.7%
General and administrative expenses	2,951	3,102	3,042	3,054	3,257	3,550	3,897	4,275	4,606
Distribution expenses	7,719	10,269	11,939	13,049	13,915	15,170	16,649	18,267	19,679
Other income/expenses	-157	246	- 154						
Operating profit	2,848	3,273	4,392	5,000	5,780	6,511	7,174	8,073	8,711
Operating margin	7.6%	7.5%	8.3%	8.3%	8.9%	9.2%	9.2%	9.4%	9.4%
Net finance costs	1,931	2,059	2,429	1,902	1,721	1,413	1,182	1,026	875
Profit before tax	917	1,214	1,963	3,098	4,059	5,099	5,992	7,047	7,836
Income tax	262	276	530	774	1,015	1,275	1,498	1,762	1,959
Net income and total comprehensive income for the period	655	938	1,433	2,323	3,044	3,824	4,494	5,285	5,877
Net margin	1.8%	2.2%	2.7%	3.8%	4.7%	5.4%	5.8%	6.2%	6.4%
Attributable to									
Equity holders of the company	588	919	1,353	2,194	2,874	3,610	4,243	4,990	5,549
Non-controlling interest	67	19	80	130	170	213	251	295	328
EBITDA	3,616	4,251	6,495	7,083	7,693	8,331	8,924	9,819	10,464
EBITDA margin	9.7%	9.8%	12.2%	11.7%	11.8%	11.7%	11.4%	11.4%	11.3%

Source: company data, Hypothesis Research estimates

Figure 82. Beluga Group Balance sheet, RUB mn

	2017	2018	2019	2020	2021	2022	2023	2024	2025
Assets									
Non-current assets									
PPE	6,501	9,898	13,885	12,749	12,134	11,664	11,641	11,689	11,800
Goodwill	230	3,511	3,511	3,644	3,783	3,915	4,052	4,174	4,299
Investment in associates	1,095								
Intangible assets	8,612	10,091	10,017	10,398	10,793	11,171	11,561	11,908	12,266
Other long-term assets	409	530	260	270	280	290	300	309	318
Deferred tax assets	1,014	1,401	1,786	1,854	1,924	1,992	2,061	2,123	2,187
Total non-current assets	17,861	25,431	29,459	28,915	28,915	29,031	29,616	30,203	30,870
Current assets									
Inventories	9,745	12,666	16,181	19,016	20,278	22,107	24,262	26,620	28,678
Biological assets	240	165	159	181	195	213	234	257	277
Trade and other receivables	11,806	8,049	9,813	11,191	12,017	13,139	14,426	15,865	17,094
Prepayments	470	595	605	690	741	810	889	978	1,054
Income tax prepayment	42	133	126	148	158	172	189	207	223
Assets held for sale	12								
Cash and cash equivalents	819	1,083	1,085	875	1,542	1,486	1,295	993	234
Total current assets	23,134	22,691	27,969	32,101	34,930	37,926	41,295	44,920	47,560
Total assets	40,995	48,122	57,428	61,016	63,844	66,957	70,911	75,123	78,429
Shareholder equity and liabilities									
Equity and reserves									
Share capital	2,495	1,940	1,940	1,571	1,571	1,571	1,571	1,571	1,571
Treasury shares	- 862	- 545	- 669	- 227	- 227	- 227	- 227	- 227	- 227
Share premium	4,957	3,760	3,339	3,339	3,339	3,339	3,339	3,339	3,339
Retained earnings	12,093	13,012	14,222	16,429	19,169	22,419	25,565	28,208	31,146
Total equity attributable to shareholders of PAO Beluga Group	18,683	18,167	18,832	21,113	23,852	27,103	30,249	32,891	35,830
Non-controlling interest	765	1,136	1,201	1,346	1,521	1,728	1,929	2,098	2,285
Total equity and reserves	19,448	19,303	20,033	22,459	25,374	28,831	32,178	34,989	38,115
Non-current liabilities									
Loans and bonds	10,112	12,419	12,628	11,367	10,367	5,367	3,367	2,993	2,620
Long-term accounts payable	-	840	580	682	727	792	870	954	1,028
Deferred tax liabilities	844	820	1,077	1,266	1,350	1,471	1,615	1,772	1,909
Total non-current liabilities	10,956	14,079	16,611	15,407	14,222	9,143	7,137	6,812	5,556
Current liabilities									
Loans and bonds	900	467	2,388	2,149	2,149	5,149	5,649	5,023	4,396
Trade and other payables	9,355	13,917	16,800	19,744	21,054	22,952	25,190	27,638	29,775
Income tax payable	336	356	364	148	158	172	189	207	223
Total current liabilities	10,591	14,740	20,784	23,150	24,248	28,983	31,596	33,322	34,758
Total shareholders' equity and liabilities	40,995	48,122	57,428	61,016	63,844	66,957	70,911	75,123	78,429

Source: company data, Hypothesis Research estimates

Figure 83. Beluga Group cash flow statement, RUB mn

	2017	2018	2019	2020	2021	2022	2023	2024	2025
Cash flow from operating activities									
Operating profit	2848	3273	4392	5000	5780	6511	7174	8073	8711
Adjustments									
Depreciation and amortisation	768	978	2103	2083	1912	1820	1750	1746	1753
(Gain) on disposal of PPE	-265	-55	22						
Share based benefits	246								
Review of estimates, impairment and revaluation	34	-22							
Other non-cash transactions	185	105	207						
Changes in working capital									
(Increase) in inventories and biological assets	-1035	-1576	-3716	-2857	-1275	-1847	-2177	-2381	-2078
Decrease in accounts receivable and prepayments	-1743	566	-1674	-1378	-826	-1122	-1286	-1439	-1229
(Decrease) in accounts payable	918	1476	3172	2944	1310	1899	2238	2448	2137
Cash flow from operating activities	1956	4745	4506	5791	6902	7261	7699	8447	9294
Interest paid	-1849	-1927	-2063	-1902	-1721	-1413	-1182	-1026	-875
Income tax paid	-578	-636	-595	-774	-1015	-1275	-1498	-1762	-1959
Net cash flow from operating activities	-471	2182	1848	3114	4166	4573	5019	5660	6460
Net cash flow from investing activities	-729	-2183	-2194	622	81	-40	-505	-517	-593
Net cash flow from financing activities	1009	265	348	-3946	-3580	-4590	-4704	-5445	-6626
Net decrease in cash and cash equivalents	-191	264	2	-210	667	-56	-191	-302	-759
Cash and cash equivalents at the beginning of the period	1010	819	1083	1085	875	1542	1486	1295	993
Cash and cash equivalents at the end of the period	819	1083	1085	875	1542	1486	1295	993	234

Source: Company data, Hypothesis Research estimates

Valuation

Beluga Group occupies a niche position being a public company in the alcoholic drinks market, the only one in Russia and one of just a few globally. Most of comparable international companies have a global presence, and benefit from a diversified brand portfolio. However, Beluga Group has already won a leading regional position in Russia and is ranked among the top global vodka players, benefiting from global distribution and a strong portfolio. Beluga Group will benefit from the still growing Beluga brand distribution, as well as from other vodka brands, and from imports growth and the expansion of the wine segment.

We value Beluga Group shares based on a DCF at an estimated WACC of 13.5% and a terminal growth rate within the range of 0.5-1.5%.

Figure 84. Beluga Group DCF model, RUB mn

RUB mn	2020	2021	2022	2023	2024	2025
EBIT	5000	5780	6511	7174	8073	8711
Less taxation	-774	-1015	-1275	-1498	-1762	-1959
Tax adjusted EBIT	4225	4765	5237	5676	6311	6752
Depreciation	2083	1912	1820	1750	1746	1753
Less: Capex	-947	-1297	-1350	-1727	-1794	-1864
Change in working capital	-1275	-796	-1074	-1227	-1376	-1172
Unleveraged free cash flow	4086	4584	4633	4473	4887	5469

Source: Hypothesis Research estimates

We have valued the company's 12-month fair market capitalization at RUB27.1-36.9bn. This translates to RUB2,208-2,926 per share, based on 12.6mn shares outstanding adjusted for

treasury shares. The sensitivity analysis for the 12-month fair market capitalization is presented in the table below.

Figure 85. Beluga Group 12-month fair market capitalization (DCF-based) sensitivity to WACC and growth rate

<i>Growth rate, %</i>	<i>WACC</i>				
	11.5%	12.5%	13.5%	14.5%	15.5%
0.0%	37339	33371	29998	27097	24576
0.5%	38670	34444	30875	27823	25183
1.0%	40126	35610	31823	28603	25832
1.5%	41729	36882	32849	29442	26527
2.0%	43500	38275	33965	30349	27274
2.5%	45467	39807	35182	31332	28078

Source: Hypothesis Research estimates

The comparable multiple analysis shows that the company trades at a 67-75% discount to global alcoholic drinks peers and a 48-71% discount to Russian and EM retail and consumer peers based on 2020-2021 P/E and EV/EBITDA. The company's share trade at 4.2-4.6 EV/EBITDA on our 2020-21 estimates and 6.1-8.0 P/E.

Shareholder capital

The Group was private before the IPO in November 2007, when the stake 19% was sold to investor for \$190mn. The common shares of Beluga Group trade on Moscow Exchange under the ticker BELU. The Group had 19.4 mn shares outstanding as of end 2019.

The Group has been executing a buyback program for several years. The total number of shares bought from the market had reached 6.69mn as of 28 February 2020. The stake 19% or 3.6mn of shares outstanding will be cancelled under the decision of the Board of directors after the approval on EGM in March 2020.

The largest shareholder of the Group, Alexander Mechetin, controlled a 47% stake before the cancellation of the treasury share stake approved by the EGM on 17 March 2020. After the cancellation of 3.6mn shares, Alexander Mechetin's effective control is to increase to 58% and the free float of the company is to grow to 17.2% from 14.0%. The remaining treasury shares represent 20.2% of the new number of shares outstanding of 15.8mn.

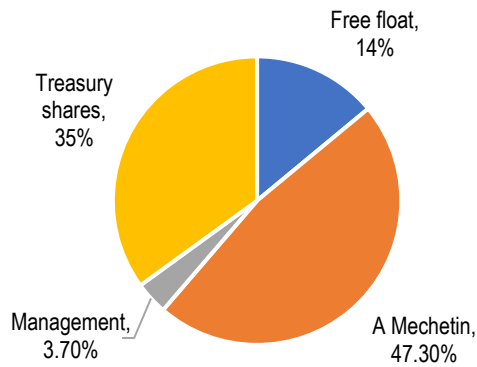
Figure 86. Beluga Group shareholder capital changes

Number of shares outstanding as of 1/1/2020	19,400,000
Treasury shares	6,690,000
Treasury shares to be cancelled (subject to EGM approval on 17/3/2020)	3,600,000
Number of shares after the cancellation of 19% stake in treasury shares	15,800,000
Treasury shares after the cancellation approved	3,190,000
Number of shares after the cancellation and adjusted for the remaining treasury share stake	12,610,000

Source: company data

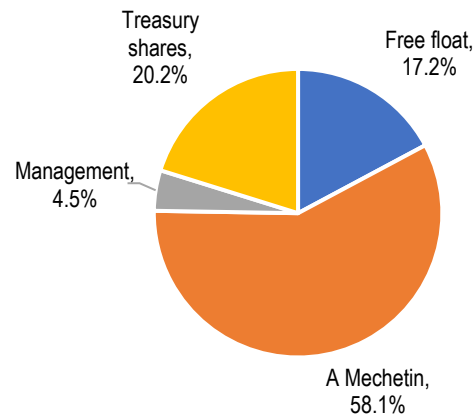
The shareholder structure after the cancellation of treasury shares is presented in the section below.

Figure 87. Beluga Group shareholder structure as of the end of March 2020



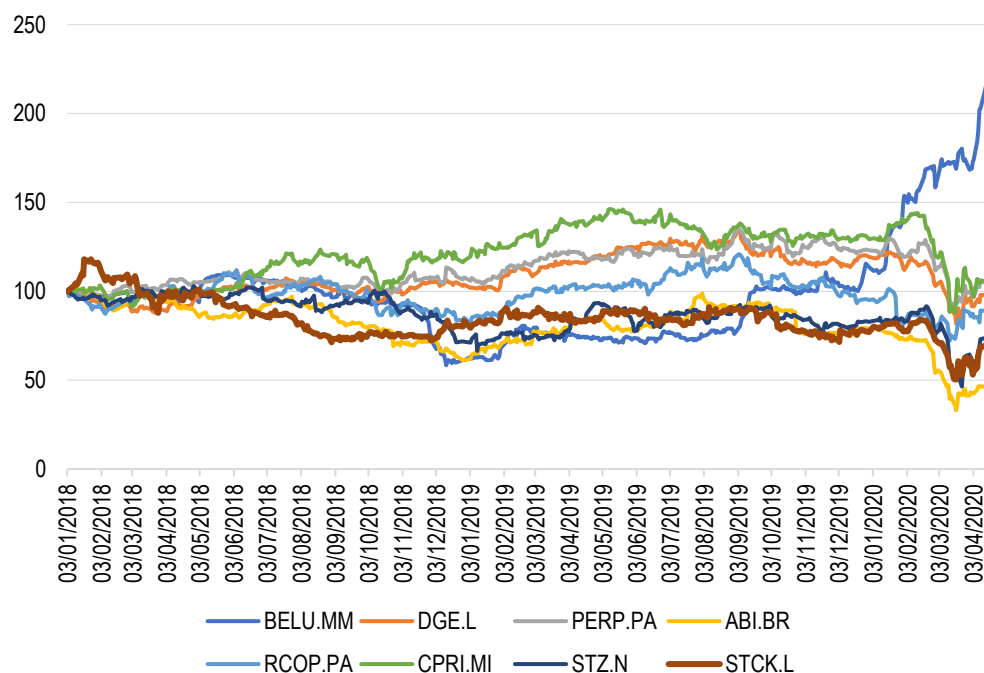
Source: company data

Figure 88. Beluga Group shareholder structure after the share cancellation (after regulatory approval)*



Source: company data, *) conditional to cancellation of treasury share

Figure 89. Alcoholic drinks peers relative price performance (03/01/2018=100)



Source: Thomson Reuters, Hypothesis Research

Corporate governance and ESG

Beluga Group operates in the challenging segment of spirits and must carry a social responsibility. The Group is involved in a number of Responsible drinking initiatives and follows all government regulations. Being a Russian spirits producer, Beluga Group has a number of local standards to meet.

Figure 90. Beluga Group ESG parameters

	Comments
Management approach	Beluga Group's corporate management is based on the following principles: 1 Push for the most efficient use of the company's assets to obtain economic profit. 2 Strict observance of the current legislation. 3 Equal treatment of all shareholders of the company. 4 Transparency of business operations, timely and full disclosure of information. 5 Attention and respect given to all parties interested in the group's activities.
Governance	
Governance structure	Beluga Group's governance structure is disclosed on the company's website. CEO of the Group, Alexander Mechetin, is responsible for the overall performance of the Group, while the Board of directors approves strategic and operational decisions and sets targets. The executive bodies accountable to the Board of Directors are the Chief Executive Officer (sole executive body) and the Management Executive Committee (collegiate executive body) that carries out the company's operational management. Additional control over the group's financial and economic activities is carried out by the internal audit department, the audit committee of the Board of Directors, an independent auditor, and the audit committee.
Delegating authority	The Group has several executive directors, each responsible for the respective area: Finance, Operations, Development and a number of regional heads in Beluga Marketing and Beluga production units. All report to the Board and CEO.
Executive-level responsibility	CEO Alexander Mechetin is responsible for the overall Group's performance. The heads of the production units are responsible for the execution of the production plans. The heads of Beluga Marketing and regional units are responsible for the performance of the sales and relationship with consumers in the regions. The head of business development is responsible for the overall development of the company's relationship with partners, customers and brands support.
Consulting stakeholders	The company has general meetings and responds to all requests online on its website to meet all questions from different stakeholder groups.
Composition of the highest governance body	The highest governance body is the board of directors which consists of seven members, including two independent directors. The Board has an audit committee.
Chair of the highest governance body	The Chairman of the Board is the executive of the company.
Nominating highest governance body	The board including is responsible for the nominations and the performance appraisal of the governance body.
Conflict of interests	The board has agreed and adopted guidelines for dealing with conflict of interests.
Remuneration policies	The company sets performance goals (KPIs) for management. The management has a combined 3.7% stake in the company and its interests are aligned with interests of shareholders. The financial remuneration is discretionary and depends on operational and financial performance of the Group.
Economic	
Economic performance	The company demonstrated a strong operating and financial performance in 2019. The Group reported RUB53.1bn revenue for 2019, up 22% YoY, and RUB6,495mn EBITDA, up 53% YoY, with net income RUB1,433mn, up 53% YoY. The company is considering the dividend pay-out.
Market presence	The Group is positioned as the leading producer of Spirits in Russia with a 12.5% share in Russian production of vodka and LVI.
Procurement practices	The Group's procurement is supervised by the BoD and executed under transparent procedures.
Anti-corruption	The Group has adopted anti-corruption policy.
Anti-competitive behaviour	The Group has adopted policies managing anti-competitive behaviour.
Environmental	
Materials	The company's materials include agriculture products and packaging. The Group is trying to minimize the use of plastics. Most of the beverages are sold in glass bottles. Paper and exclusive packaging is made using environmentally friendly materials.

Energy	Electricity consumption was 13.6 MW per year in 2019.
Water	Water consumption was 343 thousand m ³ t in 2019. The Group uses water for spirits production. The water used is produced from the clean well with extra filtering at the company's production plants.
Biodiversity	The Group has a limited influence on biodiversity, monitors and maintains the records of the impact on the production areas.
Emissions	The Group has limited emissions and tries to minimize the impact every year.
Effluents and Waste	The Group's waste of the Group was 2180 t in 2019.
Environmental Compliance	Both the environmental impact and air quality at the boundary of sanitary protection zones are being continuously monitored for compliance with the established limit values across all Beluga Group's production sites. These factors are assessed by designated organizations on a quarterly basis. Usable industrial waste is collected for recycling, while hazardous waste is disposed of by designated companies.
Supplier Environmental assessment	Beluga Group complies with Russian environmental laws and regulations and seeks to minimize the environmental impact of its production process and waste. The company's key environmental protection activities involve sustainable use of natural resources, saving energy, recycling a range of materials, and proper industrial waste disposal.
Social	
Employment	The group employs over 10,500 people, with 2,000 working in sales. Over 80% of new hires enroll in the adaptation program.
Labour / Management relations	The group's staff policy is primarily focused on creating new incentives, providing objective assessments of each professional's share of contribution to the company's success and supporting and developing intrapreneurship and talents as well as creating opportunities for career and professional growth and self-realization.
Occupational Health and Safety	The Group has high standards of occupational health and safety and meets all local government standards.
Training and Education	In 2018, the company employees completed over 85,000 distance learning courses. More than 500 professionals upgrade their qualifications annually. More than 160 courses are available via the distance learning platform. Some 60 senior executives completed their training at the Moscow School of Management SKOLKOVO. On top of that, some 250 key employees and their successors accomplished a comprehensive middle management training program.
Diversity and Equal Opportunity	The group promotes diversity and equal opportunity. The women represent 60% of employees.
Non-discrimination	The group promotes non-discrimination.
Freedom of Association and Collective Bargaining	The Group does not have unions or other employees' organisations. The employees represent the best asset of the Group and the management takes care of the education, adoption plans and remuneration of employees.
Child Labour	The company has strong policies prohibiting child labour.
Forced or compulsory labour	The company has strong policies prohibiting forced labour.
Local communities	Beluga Group is supporting social action projects. These include the Zarya Center for Contemporary Art in Vladivostok, a non-profit organization, aimed at promoting the best of art from Russia and beyond as well as providing support to young artists and the professional artist community.
Public Policy	The company cooperates closely with the Federal Service for Alcohol Market Regulation and takes part in the development and implementation of joint initiatives to facilitate a general improvement of drinking culture and to establish a civilised and productive cooperation between the market players.
Customer Health and Safety, Marketing and Labelling	According to the company's statement, "We never promote drinking; instead, we offer quality products to adult consumers who have already made their informed choice in favour of a product made by our Company or are about to do so. BELUGA GROUP's marketing activity fully complies with the requirements of the Russian law."

Source: Company data

The Board of directors has seven members, including two independent directors. The Board of Directors is responsible for general management matters and determines the company's strategy.

Figure 91. Beluga Group Board of Directors

Alexander Mechetin CEO, Member of the Board Age: 44	Alexander Mechetin is the founder of Beluga Group and has been its leader for over 20 years. He graduated from the Institute of Economics and Management of the Far Eastern State Technical University, holds a Law degree, a PhD in Economics, and received an EMBA from Oxford University.
Nikolay Belokopytov Chairman, CFO Member of the Board Age: 44	Nikolay Belokopytov has served as an executive of Beluga Group for the last 19 years. He is Chairman and CFO of the Group. Mr Belokopytov graduated from the Institute of Economics and Management of the Far Eastern State Technical University.
Mikhail Kashirin Deputy Chairman for Development, Member of the Board Age: 46	Mikhail Kashirin has been with the Group for the last 13 years, including 7 years in executive positions. He graduated from the All-Russian State Distance-Learning Institute of Finance and Economics with a marketing degree.
Sergey Molchanov COO Deputy Chairman Member of the Board Age: 43	Sergey Molchanov has held executive positions with the group's companies for the last 18 years. He serves as COO of the Group. He graduated from the School of Economics of the Far Eastern State University and holds a Bachelor's degree in management from the University of Maryland University College (USA).
Konstantin Prokhorov Director general of WineLab-Zapad LLC Deputy Chairman Age: 41	Konstantin Prokhorov joined the company over 13 years ago, holding executive positions since then. He graduated from Primorsk State Academy of Agriculture with a degree in Economics and Management of Agricultural Production.
Rostislav Ordovsky-Tanaevsky-Blanco Independent director, Member of the Board Age: 61	Rostislav Ordovsky-Tanaevsky Blanco serves as an independent director of the Group. Mr Ordovsky-Tanaevsky Blanco is a founder of Rostik International in Venezuela and the Focus company, the distributor of Kodak group in CIS in 1980s and Video Express and Bradly, which were distributors of Walt Disney in Venezuela. He founded Rosinter Restaurants Holding in 1990, which became the largest restaurants chain in Russia and became a public company in 2007. Currently Mr. Ordovsky-Tanaevsky Blanco is President of RosKorp LLC. He holds a degree in Chemical Engineering from Simon Bolivar University (Caracas).
Alexander Ikonnikov Independent director, Member of the Board Age: 48	Alexander Ikonnikov is non-executive director of the group. He serves as Director General of Board Solutions. Mr Ikonnikov graduated from Gubkin Russian State University of Oil and Gas and has a PhD in Economics. He holds an IoD Chartered Director qualification.

Source: company data

Beluga Group has a dividend policy, according to which the company may pay a quarterly or an annual dividend, based on the net income reported in accordance with Russian Accounting standards. The payment has to be approved by the Board.

Risks

- Worsening macro trends due to the COVID-19 threat.
- Decreasing numbers of people travelling due to COVID-19 will result in drop in Global Travel Retail volumes.
- The Russian macro environment is changing in 2020 following the OPEC+ deal cancellation and drop in oil price.
- Russian consumers may switch to cheaper beverages from premium alcoholic drinks.
- Changing regulatory environment, including changes in taxes and excise duties may affect the Group's business.
- Financial leverage may influence the dividend pay-out decision if cash flows weaken.
- The new products promoted by competitors and cheaper alternatives may affect the Group's market share in the Russian Spirits market.
- Changes in the FX rates may negatively influence the cost of imported materials.
- The company's margin may be affected by price wars in the weakening macro environment.

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