SOFT DRINKS IN EAST AFRICA

Still or sparkling?

RANGE OF RESEARCH

This report is descriptive in nature and focused on analysing the soft drinks market in East Africa.

Our publication presents the current situation of the market and gives a comprehensive overview of the macroeconomic environment, regulatory environment affecting the industry, the value chain of soft drinks, trends influencing the market, competitive landscape and opportunities we have identified. The research describes key ready to drink soft drinks categories – from carbonates, to energy drinks, bottled water as well as juices. We are aware that East Africa has a traditional beverage market as well as large tea and coffee sales however from a ready to drink perspective, these categories have been excluded as sales volumes are low.

In order to provide a comprehensive picture, the primary data-collection method employed was engagement with Standard Bank's Consumer Sector teams in country; we also interviewed soft drinks consumers, producers and distributors across East Africa. Third party information was also used in the process. Our approach was to spend time walking the streets, understanding the soft drinks market and client preferences in their environment.

This study is delimited to three countries in East Africa; Kenya, Tanzania and Uganda. When reference is made to East Africa, we are mainly referring to the three countries listed above unless otherwise stated.

This report contributes to Standard Bank, Consumer Client Coverage's mission to help businesses understand the African Consumer sector. We hope that our report will provide you with the convincing insights into the soft drinks market in these countries.

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FOREWORD

Emerging markets and Africa, in particular, are demanding places to invest. Received wisdom would have many desk-bound Economists committing an error in judgment when just focusing on the micro and macro published data for Africa. Sitting behind a desk and modeling consumer trends from a computer can be useful. However, nothing brings consumer trends to life better than a real-world trade visit.

What you are about to read through is a summary of a journey into key African markets, with the challenge set at gaining a deeper understanding of the non-alcoholic ready to drink beverage market of Africa based on real experiences and primary research. While we hope to capture as much of our findings in this accessible thought piece, some critical topics require further study and analysis, and more importantly greater focus by corporates and countries alike.

The reality we, as consumers and stakeholders of the planet's resources, now face is a lot more challenging. The science and data clearly shows we can no longer continue on this consumerism journey at all expenses. Global corporates are being forced to acknowledge this and make changes through dramatic shifts in their operating models. The algorithm for success no longer involves profits and dividends to shareholders, but rather a broader approach to improved stockholder values and needs.

Africa is a continent that will grow its population of youth by 42% over the next ten years and is still viewed as a destination for growth capital. In the consumer sector, the potential for growth is driven by increased population, urbanization and improving median incomes. The growth remains the driver for future investment. However, a focus on profitable investment at all cost can no longer be the mantra.

Africa has for far too long been the playground for large corporates and countries to arrive on this beautiful, raw and natural landscape, to play the game of resource extraction with no recourse to the disaster that is left in the form of limited value uplift to Africa's people and absolutely no rehabilitation to Africa's environment.
The future for the continent needs more focus on resource extraction with a view and investment in replenishment and value creation for the continent.

This document draws attention to one particular part of the growing consumer sector and has been developed to highlight opportunities and risks, but also to enhance debate around the fundamentals of future investing.
Standard Bank has invested heavily behind the consumer sector and has a specialized consumer team that is like no other on the continent. The model we have adopted is one of partnership, as we look to work with our clients to understand the opportunities, risks, and realities of investing in Africa. Our clients are corporates, but they also include all stakeholders in the process of analysis. This holistic approach of consulting on the future means that we hold true to our values as a company but also to our values as global citizens and how decisions impact on all stakeholders.

As you read through the opportunities that we have discovered in the African beverage sector, you will see the risks and potential challenges that stakeholders are facing. While certain regions in Africa present significant growth opportunities in the beverage space, they are also currently the highest risk areas in terms of negative externalities and will require innovative and bold leadership to change the future of success in the industry. Something that up to this point in time has been drastically lacking on the African continent.

Areas of concern include an all-encompassing focus on profitability in the category centered behind fast-growing beverage products that may not be very good for consumers health, as well as massive shifts into cheaper plastic packaging that is most definitely not good for the health of the environment.

Trends that we see in Africa are in line with global trends. We are living through an age of disruption in the global consumer sector like we have never seen before. Global consumer multinationals are having to self-disrupt to remain relevant as their traditional thinking and scale production no longer is meaningful to what consumers want and need. The need for change has already resulted in six of the top Consumer Packaged Goods companies replacing their CEOs in the last two years.

Relevance is something companies now need to discover once again, as their products, brands, meaning, and packaging strive to enhance consumer intimacy.

Emerging markets continue to be the focus for growth as many disruptive trends are yet to impact the positive macro trends that still underpin expansion. China and Brazil continue to lead with consumer packaged goods growth rates surpassing many of the multinational corporates home markets. Sector trends in dairy (yogurt), beverages and convenience packaged foods (snacks) require a focused and patient strategy as these are often in contrast to what is happening in developed markets.

The reality is that patience has often been lacking on the African continent, and this has been to the detriment of long-term investment capital. We hope that this document and others to follow will stimulate a debate and further analysis around the allocation of capital and required returns as they are weighed up against growth. Certain sectors continue to present good return opportunities for all stakeholders, but they require measured and mindful investment.

Brendan Grundlingh – Standard Bank Consumer Sector
Global Head, Consumer Packaged Goods

KEY FINDINGS

Overall, we find a vibrant soft drinks industry with numerous competitors competing across the key categories predominantly on price to the immense benefit of consumers. While challenges remain in terms of distribution and accessing the full potential of the region, there are opportunities for further growth in the market as incomes rise and tastes continue to expand.

The soft drinks market in East Africa is worth USD 800 million …

Africa accounts for just 3 percent of global soft drink consumption with Nigeria the biggest consumer in the region. Kenya has experienced the fastest growth in the past decade and East Africa has arguably the most vibrant regional soft drinks market.

Carbonates are the key category, but water and juice cannot be ignored

Carbonates account for 71 percent of soft drink consumption in the region and is expected to grow further, unlike many regions across the world. Water and juice are sizable with favourable growth dynamics.

120 million people relying on the successful implementation of the East African Community

Rising FDI flows support the positive outlook for the consumer in the region but the EAC needs further support for companies to unlock the regions' true potential.

Coca-Cola is the key regional player but local competition is fierce

The Coca-Cola Company is the key player in the region, leveraging its long history, brand and distribution capabilities but key local players have provided fierce competition and have managed to significantly grow their market share.

Distribution remains the key competence in the value chain

In what remains a large traditional retail market, distribution remains a key competence for bottlers attempting to reach vast populations in a profitable manner.

Opportunities to consolidate and innovate exist

The market has been led by price and category innovation, and we believe there exists further opportunities to innovate. In addition, the industry is at differing stages of consolidation, with juice and water categories most ready for further consolidation.

Trends in the region are broadly in line with global trends

Concerns around packaging and ever-lower prices characterised the industry, much like the rest of the industry but health is a surprisingly strong trend

SECTION 1:

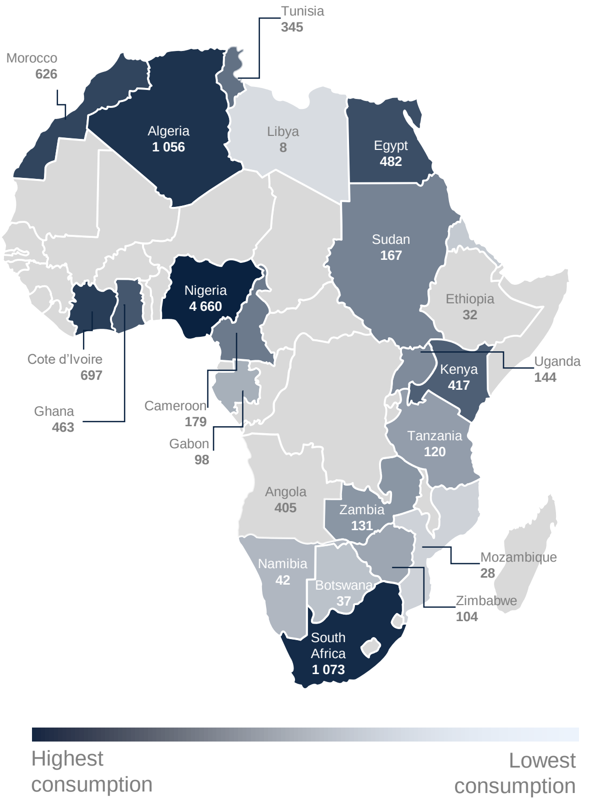
Global Soft Drinks Market worth USD500 billion

The global soft drinks industry is worth an estimated USD 295 billion and will grow to an estimated USD 377 billion by 2023. On a value basis, Asia and Europe account for around 29% of consumption each, while Asia's growth will outpace the rest of the world for the next five years at least.

Despite accounting for 16 percent of the global population, rising to 25 percent by 2050, Africa accounts for just 3 percent of the total value of soft drinks consumed across the world. By 2023, this will rise to 3.9 percent. West Africa, driven by the single largest consumer, Nigeria, is currently the largest regional consumption hub in Sub-Saharan Africa.[1]

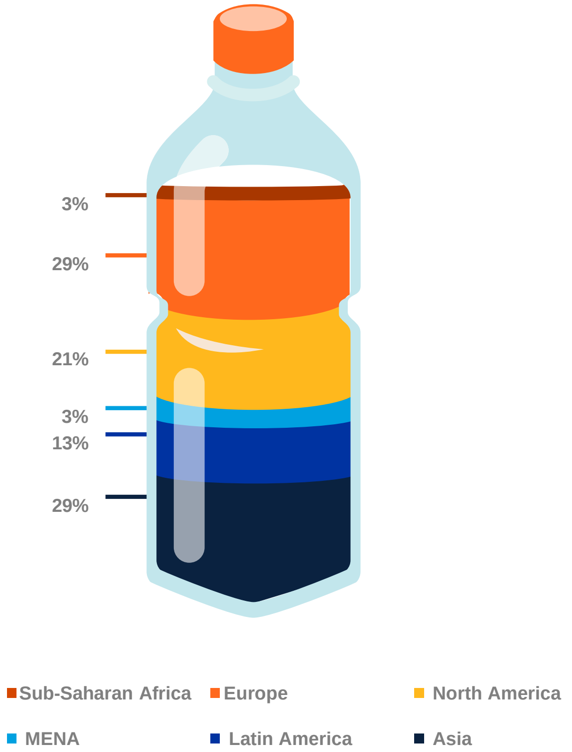
Between 2008 and 2018, Kenya showed the fastest consumption growth in Sub-Saharan Africa, recording a 10.6 percent CAGR in USD terms, followed by 7.7 percent in Angola

Africa Soft Drink Consumption 2018 (USD'm)

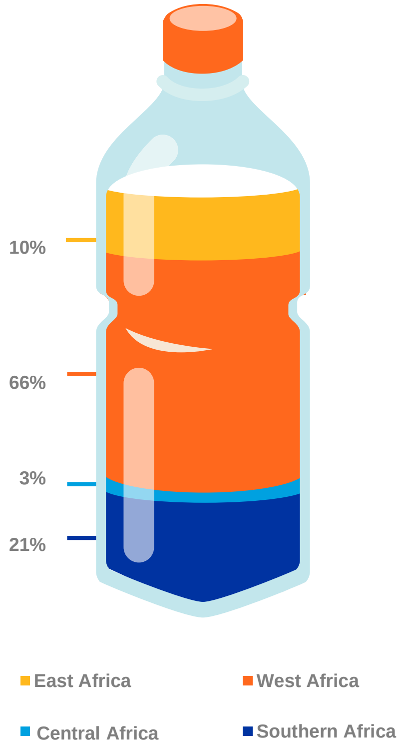


Source: Fitch Solutions

Soft Drink Sales: Global (2018)



Soft Drink Sales: Sub-Saharan Africa (2018)



Source: Fitch Solutions

[1] Fitch Solutions. "Global Food and Drink Report." London, 2019.

Sub-Saharan Africa – Still attractive, despite challenges

The Sub-Saharan growth story has been well-documented. Home to large populations, some of the fastest growing economies across the world and ever-improving fiscal and political environments, it has witnessed surging investor interest, across all industries, including consumer.

Much optimism for Africa rests with the "growing middle-class" narrative. Whilst there are numerous estimates of the number of middle-class households and indeed the criteria for middle-class itself, the consensus view is that the middle class will swell in coming years. Standard Bank analyst Simon Freemantle expects the number of middle-class households to surpass 40 million by 2030, from 15 million today.[2]

Recent years have seen a continent restricted by depressed commodity prices, uncertain policy conduct and a period of negative sentiment towards emerging markets as global growth accelerated. Looking forward, the balance of risks points to a continuation of the moderate acceleration in economic growth across the continent. There are some notable downside risks that might depress growth in some countries, but overall it seems highly likely that there will be a modest acceleration in growth on the continent.

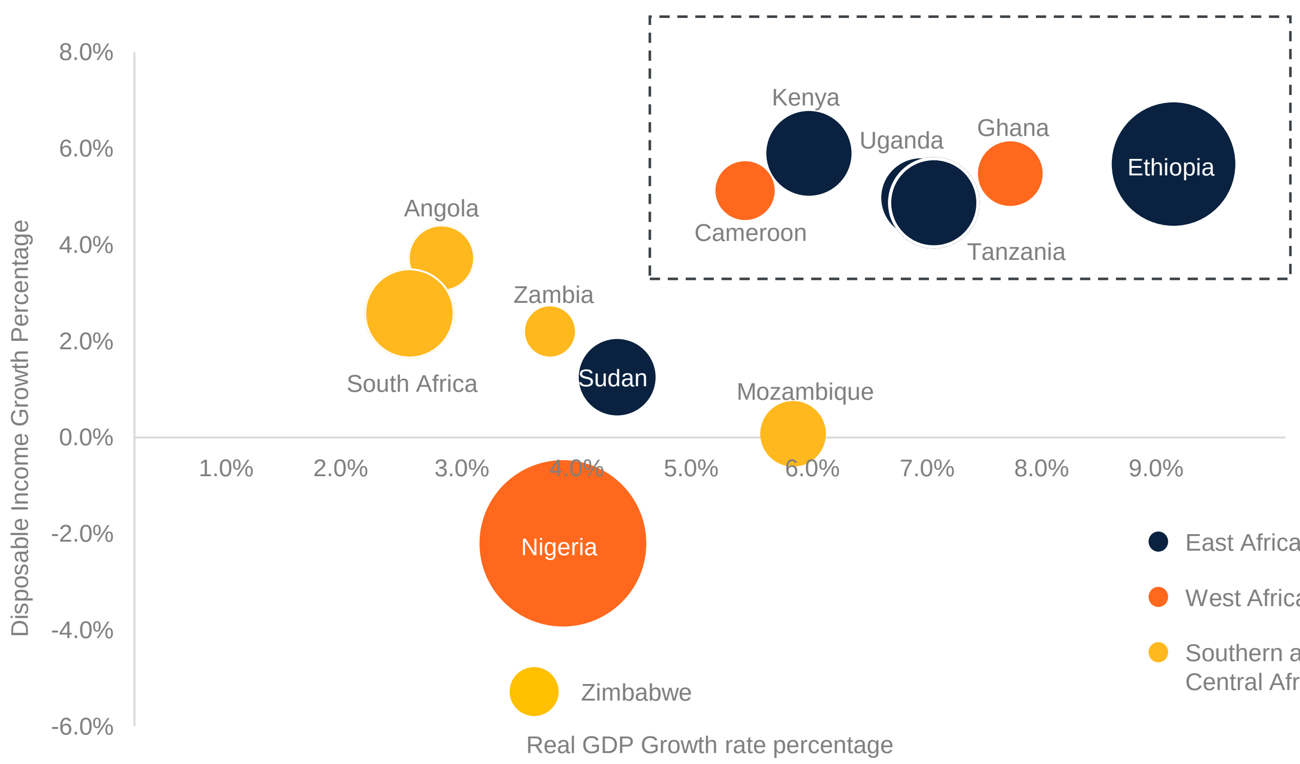
East Africa to increase in significance

Looking regionally, the East African growth outlook is potentially most rosy. Limited exposure to the oil price slump, a benign political environment and a relatively business-friendly environment has seen numerous global consumer companies establish a presence in the region.

Going forward, GDP growth expectations across the region's key countries are among the highest in the world. Coupled with fast-rising consumer incomes, East Africa, led by Kenya, is well-positioned for growth.

Higher incomes are naturally supportive to higher soft drinks consumption but have additional benefits for the industry. Higher household budgets sophisticate meal consumption, allowing for higher meat consumption and more occasion meals among families. This not only supports consumption growth but drives a sophistication of consumption as consumers seek a greater variety of tastes.

Comparison of disposable income growth to GDP growth



Source: Economist Intelligence Unit

Bubble Size represents population

[2] Price-Waterhouse Coopers. "Prospects in the retail and consumer goods sector in ten Sub-Saharan countries." 2016.

Regional consumption patterns

Comparing category consumption across countries provides valuable insight into the “beverage culture” across the continent. Traditionally, specific countries are often associated with specific drinks, for example tea in China or beer in Belgium.

Globally, there has been a shift away from single profile beverage cultures as globalisation has increased consumer expectations and awareness. Multi-profile beverages cultures – where more than one category holds a strong market share – are becoming increasingly prevalent. Mexico is a prime example. Its carbonates market is the second largest in the world, yet water drives double the volume and beer has the biggest value share across the industry. Three categories each enjoy their own high-profile consumption.[3]

In Nigeria, the biggest Sub-Saharan African market, nearly 95 percent of consumption is in bottled water, owing to a combination of poor water supply, lack of affordability and extremely hot weather conditions.[4]

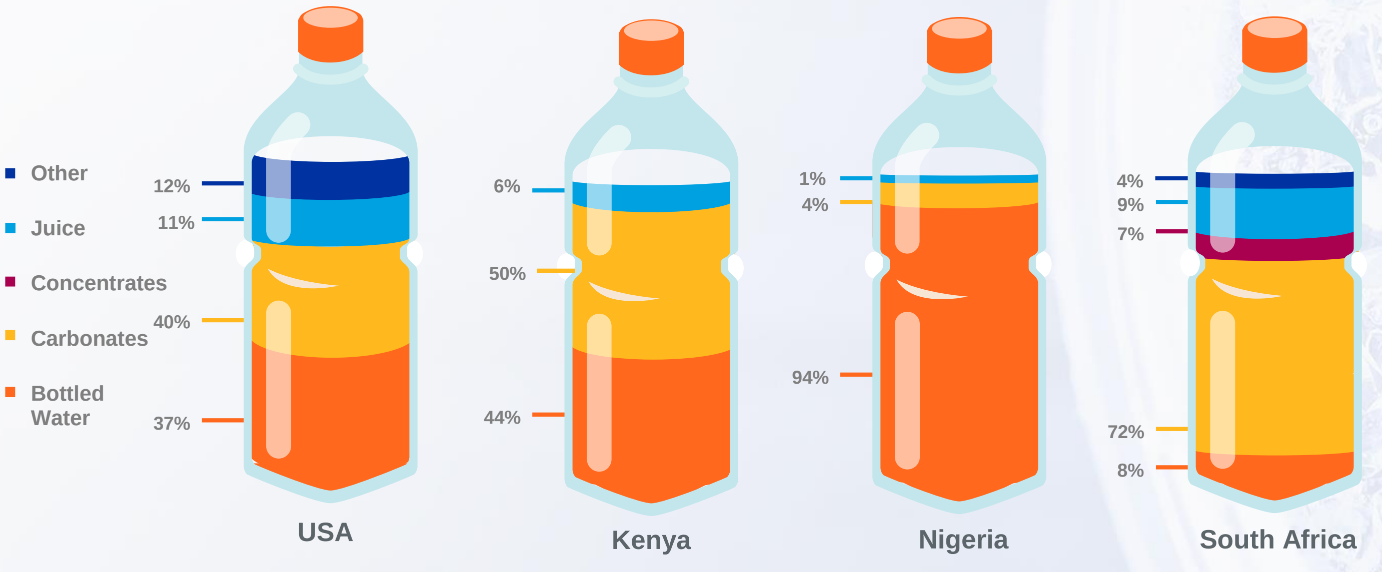
Carbonates account for just 4.3 percent of Nigeria’s 44.1 billion litres of consumption in 2018 – 1.8 billion litres. As a result, despite being a market 51 times larger than Kenya, its carbonates consumption is only 4 times bigger.

In contrast, carbonates account for 72 percent of consumption in South Africa. Despite economic constraints and shrinking disposable incomes, a highly competitive environment has kept prices steady. The sugar tax implemented 1 year ago has received criticism, mainly from sugar producers as the legislation has cost drink producers ZAR1.5 billion in revenue and a 30 percent reduction in sugar usage.[5, 6, 7]

Consumption in Kenya is most like that of the US, with a near even split between carbonate and water consumption. Additionally, the juice category makes up 6.1 percent, a sizeable split compared to Nigeria. This category variety is driven in part by a strong mall culture which creates a showcase effect for consumers – regularly displaying new brands and categories far in advance and with greater regularity than traditional traders.[8]

We believe this greater category variance increases the attractiveness of a market and is an indicator of greater market maturity - creating more opportunities for companies to enter the market and provide unique offerings.

Consumption by Category (2017)



Source: Euromonitor International

[3] Euromonitor International "Drinking Cultures of the World – Globalisation Creates Opportunities – World." London, n.d.
[4] Euromonitor International. "Soft Drinks in Nigeria." 2018.
[5] Euromonitor International. "Soft Drinks in South Africa." London, 2019.
[6] USDA Foreign Agricultural Service. "South African Sugar Industry Crushed by Not So Sweet Tax." 2019.
[7] Stainbank, Graeme. *Sugar tax is a bitter pill — and there's no evidence it will curb obesity* (March 10, 2019).
[8] Euromonitor International. "Soft Drinks in Kenya." 2019.

Consumption per capita – Large upside potential

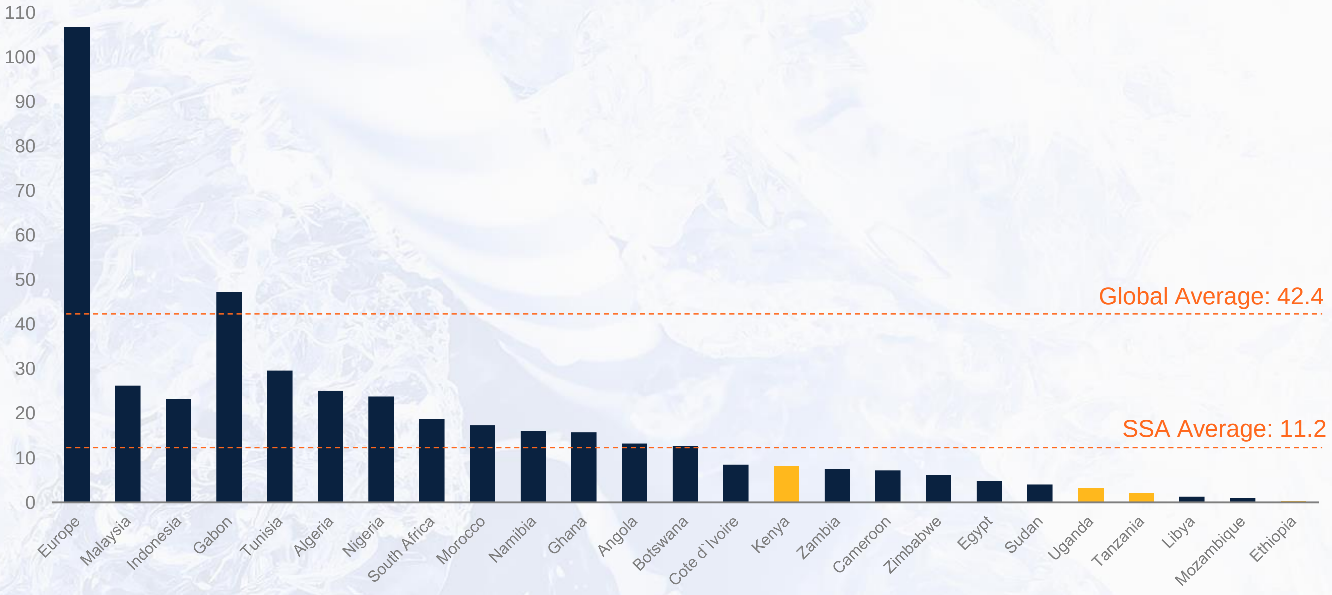
Global soft drink consumption per capita on a value basis is USD42 per annum and is expected to grow by 4.3 percent CAGR from 2019E-2022E, reaching USD49 per annum.

Regionally, North American soft drink consumption, at USD178 per annum is significantly ahead of second placed Europe. Comparatively, Sub-Saharan Africa sits at a meagre USD11 per annum, but will be the second fastest growing region, behind Asia.

On a country basis, only Gabon is ahead of the global average, at USD47 per annum per capita consumption.[9]

Interestingly, Ethiopia, Tanzania and Uganda are all below the Sub-Saharan Africa average. This is as a result of a limited numeric distribution and price points that make soft drinks a luxury purchase. In our view, this presents a significant upside with significant opportunity for companies who can solve these equations to benefit from the large consumer bases.

Soft Drink Consumption Per Capita 2018 (USD)



Source: Fitch Solutions

[9] Economist Intelligence Unit. n.d.

SECTION 2:

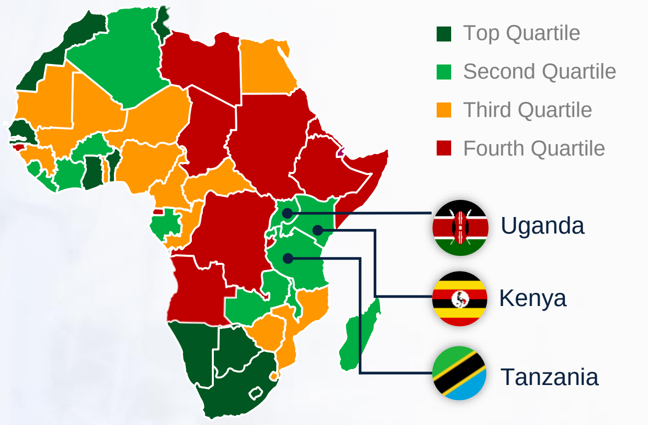
The landscape is shaping up and making it easier for investors to participate

Readiness for growth is indicated through ease of doing business and positive FDI flows

East Africa is gearing up for growth in the consumer sector. Two indicators which strongly back this sentiment are general increased ease of conducting business, as well as an increase in FDI focus within the sector.

The region has shown commendable progress and is positioned in the top 2 quartiles in Africa from an "Ease of Doing Business" perspective. East Africa has implemented numerous business reforms that have fundamentally transformed how easily businesses can operate in the various countries. Kenya has seen the greatest improvement in the region. In just two years the country implemented over ten reforms-the highest in Sub-Saharan Africa, and resultantly moved up 31 positions on the Doing Business ranking scale (from 92 in 2016 to 61 in 2018).[10]

Ease of Doing Business landscape in Africa



Source: U.S. Chamber of Commerce

Data shows that countries with business-friendly policies and conducive reforms are most successful in outperforming their peers in attracting foreign investment. A direct correlation between FDI projects and the absolute size of a country cannot be ascertained. This can be evidenced from Nigeria, Angola and Egypt, all of which attract little by way of FDI projects, despite them being some of the largest countries on the continent and Rwanda, with an economy only one-tenth the size of Angola's, receiving more FDI projects in both relative and absolute terms.[11]

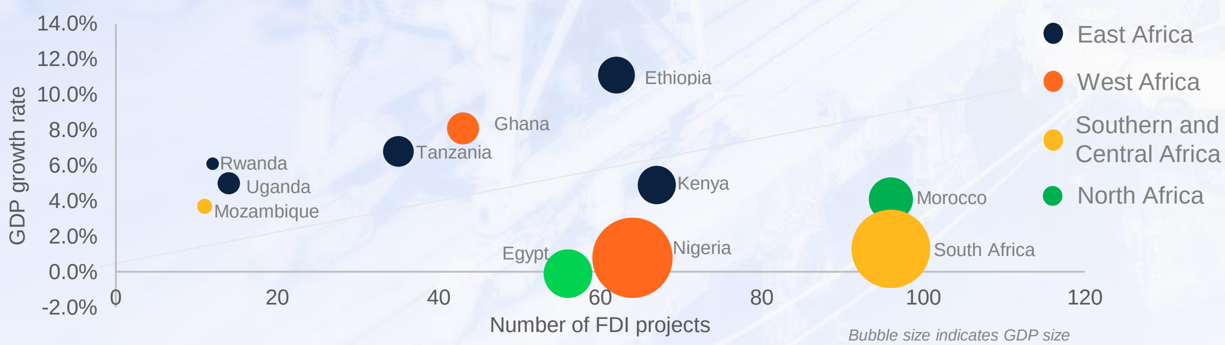
In order to drive investment growth, governments need to put more focus on policy reform and drive an agenda that stimulates and supports private sector economic activity.

In East Africa, overall FDI shows an upward trend and has grown by almost 5.5% over the last decade[12]. For the first time ever, it became the single largest beneficiary as a region for FDI with 197 projects (27% of total projects) between 2016 and 2017."

We have observed the changing investment landscape and note that FDI is starting to diversify into consumer industries including consumer products such as packaged food and retail. The shift in focus has had an impressive impact on the region. Between 2003 and 2014, the packaged goods and retail category in East Africa, received either the highest, or second highest investment allocations in the manufacturing sector[13]. In 2017, Ethiopia became the fastest growing economy as well as the fifth largest recipient of FDI projects with consumer packaged goods and retail making up a quarter of these projects. In 2017, Diageo boosted FDI in Kenya with a USD14 million investment into a new spirits distillery in Nairobi and in Tanzania, *Anheuser-Busch InBev* has plans of investing USD100 million in a new brewery which will be strategically situated in the city of Dodoma. *PepsiCo* invested USD30 million into a plant in Nairobi and *The Coca-Cola Company* plans to invest USD100 million over the next five years in Kenya.

Countries in Africa which received the most FDI projects (2017)

Countries positioned above the line attract proportionally more FDI than those below it.



Source: qz.com; BMI Research

[10] Trading Economics;. (2019). Ease of Doing Business in Kenya. Trading Economics. Retrieved from https://tradingeconomics.com/kenya/ease-of-doing-business
[11] EY. (2018). *Turning tides: EY Attractiveness Program*. EYGM Limited.
[12] Data sourced from 2019 BMI Research
[13] World Bank Group. (2015). *Manufacturing FDI in Sub- Saharan Africa: Trends, determinants and impact.* Washington, DC 20433: World Bank Group.

The East Africa Community: great in theory but still needs implementation

The main purpose for the establishment of the EAC is to facilitate regional trade. The community has established unions and policies which aim to improve trade and supply chain efficiencies for market players who aim to reach the 191 million citizens in this region.

To achieve economies of scale in African distribution networks, most companies adopt a regional approach

Companies wishing to dominate the African continent have been observed to approach it from a regional perspective. *The Coca Cola Company* for example, first set up shop in Kenya in 1958. Five years later, once the brand had become entrenched in the market, it moved to Uganda and then to Tanzania. Local players are also adopting a similar strategy. In Tanzania, companies like *Bakhresa Group* and *MeTL Group* have been discussing plans of expanding/ distributing their beverages into Kenya, Uganda and Rwanda.

When taking on a regional approach, one of the most important things to consider, especially when preserving supply chain efficiencies, is having regional integration. Regional integration from an African context entails the establishment of government agreements to facilitate intra- regional trade. Globally, Africa is the least integrated continent (at 18 percent) compared with Europe (70 percent), North America (55 percent), Asia (45 percent) and Latin America (35 percent) respectively.[14] Although many Regional Economic Communities (RECs) exist, not all have been successful. The EAC has gained the most traction.

The EAC is an *intergovernmental organisation,* **headquartered in Arusha, Tanzania**

One of the most impressive ways in which the EAC aims to achieve these efficiencies is through the establishment of the *Customs Union Protocol.*[15] This protocol aims to enforce free trade on goods flowing within the region. In theory, *The Coca-Cola Company* for example, has bottlers operating in Tanzania and Uganda who import their mango pulp from Kenya. Through the Customs Union the pulp moving between Kenya, Tanzania and Uganda as well as the equipment and other raw material purchased, transported/ imported within the region (and used in the beverages production process), should be tax- exempt.

In the current trading reality, the implementation of the EAC stills needs more development and more than anything, the implementation of the community's protocols and policies in order to open regional borders.

[14] Akorede, S. (2018, February 28). *How a single market would transform Africa's economy*. Retrieved from World Economic Forum: https://www.weforum.org/agenda/2018/02/how-a-single-market-will-transform-africa-s-economy/
[15] East Afrca Community. (2019). *Customs Union.* Retrieved from East Afrca Community: https://www.eac.int/customs-union

SECTION 3:

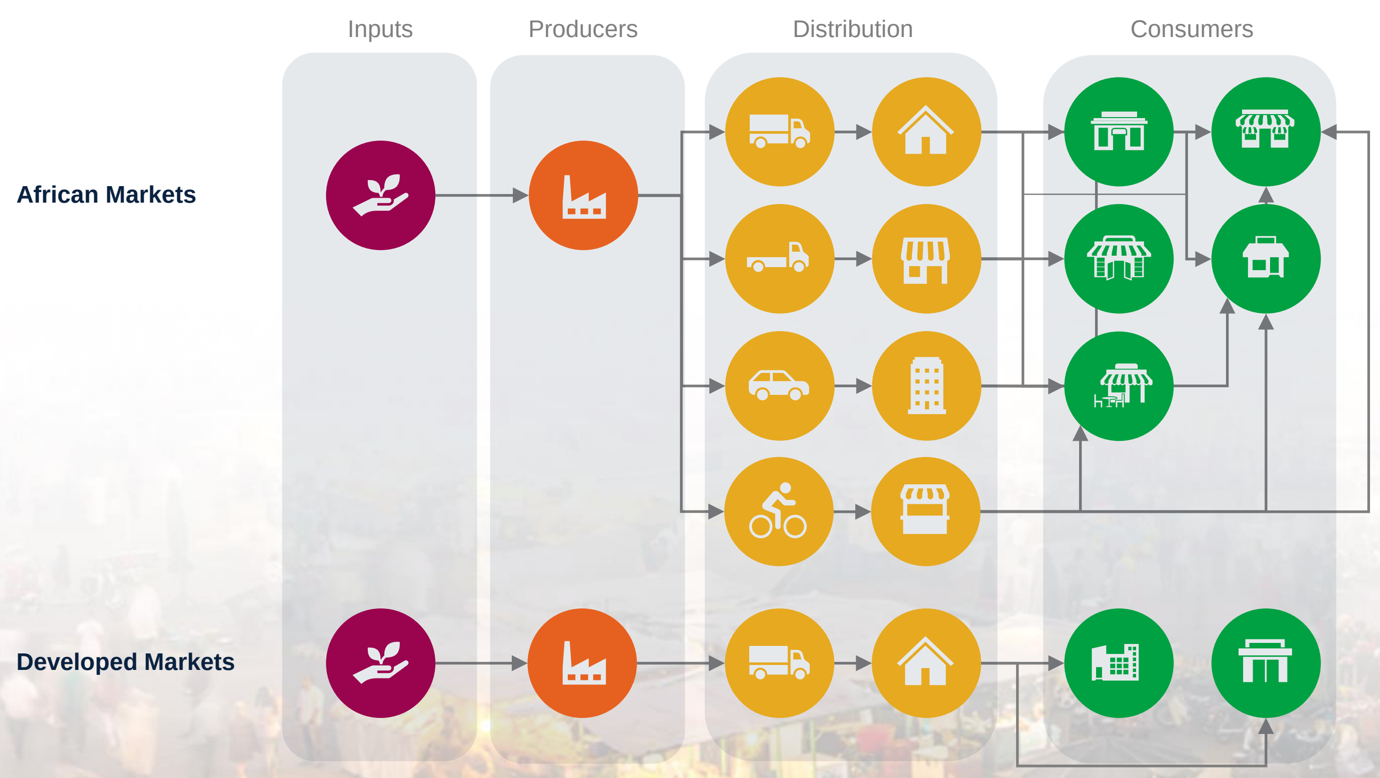
The Soft Drinks value chain – distribution the core competence

Globally, retail supply chains have faced increasing pressure to deliver as retail behemoths such as Amazon pull consumers into expectations of wide online assortments and same day delivery. In stark contrast, consumer companies in Africa continue to face significant physical challenges in producing products in and delivering them to a highly fragmented end consumer. This is especially true in an environment of price elasticity and vast land areas. The beverages market is particularly exposed, where margins are narrow and required volumes, large.

In this section, we unpack the current value chain, which we split broadly into production and distribution. In our view, distribution remains the single biggest hurdle that new and existing companies must contend with, with efficient distribution key to reaching a vast population in a profitable manner.

We unpack a value chain of import reliant production, with fragmented distribution to an end consumer that is slowly shifting away from viewing soft drinks as a luxury purchase.

Distribution Pyramid



Production – Currently relying on imports

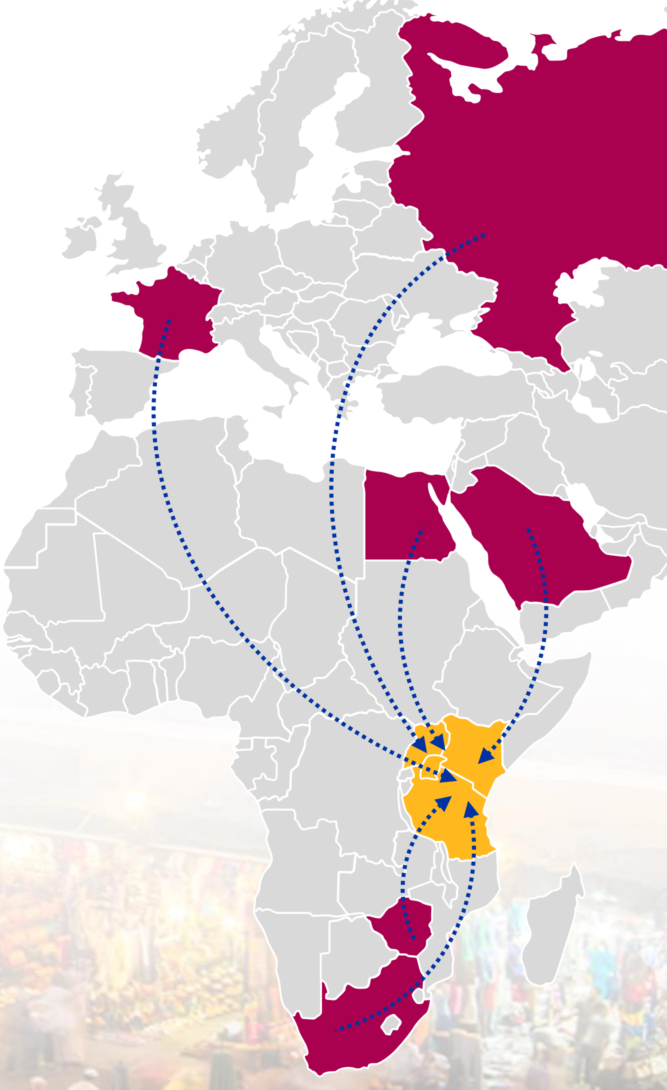
The soft drinks production process is characterised by inputs that are nearly completely imported, creating a risky revenue mismatch for both local and global market participants.

The key inputs – sugar and concentrate, are imported, mainly from other African countries or the Middle East. Together they account for 80 to 95 percent of the direct cost of production. Sugar is imported primarily from the Middle East. A lack of local availability coupled with no refining capability in the region drives this requirement. Sugar consignments being stuck at ports awaiting clearance has been a regular concern for Tanzanian manufacturers, leading to instances of critical shortages and temporary shutdowns at several carbonated soft drink plants.

In the juice category, local players are increasingly able to source local pulp with superior access to pineapples and mangoes in particular. However, *Coca-Cola Bottlers Africa* (the key multi-national player in the region) continues to import significant quantities of pulp from around the world – oranges from South Africa and apples from France. In 2018, it announced its intentions to source 80 percent of its raw material input locally by 2022. This has started in earnest in Uganda where it has begun working to develop a local supply of fruit pulp to meet its 5000 ton annual requirement.

A note to the two opposing production options in the juice category – end-to-end in-country production versus pulp importation. Whilst the importing of pulp introduces foreign exchange risk, it does simplify the in-country production process. A tour of a local leading juice manufacturer in Tanzania illustrated the sheer vastness of an end-to-end juice facility. In addition to the bottling element, facilities need to allow for raw fruit acceptance, ripening facilities and storage. The capital requirements should not be underestimated.

Whilst large elements of the production process are somewhat generic, a low barrier to entry, concentrate for carbonates has presented an opportunity for local players to expand the flavour offering of their brands beyond the reach of the global players, *The Coca-Cola Company* and *PepsiCo.* Whilst international players have largely stuck to the "original" brand offering, local players in Uganda and Tanzania have captured consumer interests by introducing unique flavours, such as apple mint and vanilla cola flavours at competitive price points.



Distribution – Going further than the state

90 percent of retail in Africa is conducted through informal channels characterised by being highly fragmented and difficult to reach. This has shaped the key challenge for consumer companies on the continent when attempting to reach as many end consumers as possible.[16]

Generally, bottlers make use of distributors who service specific areas, in an effort to manage location-specific challenges and consumers. Bottlers either manage this chain completely, from bottling to selling to the end consumer or use third parties, previously mandated by law in Kenya. In our view, the degree of control that bottlers exert over independent distributors is not too dissimilar to ownership, so we find little difference between the two. If anything, the entrepreneurial element introduced by independent bottlers provides some benefit to the latter model.

Distributors are tasked with being the day-to-day face of the brand and providing products to a specific territory. These territories vary in terms of size, but in dense urban areas can be as small as a couple of blocks. Independent or not, they are only allowed to stock one brand of beverage and in many cases, cannot distribute other products, regardless of category, from the same warehouse. Transactions between bottler, distributor and end retailer are entirely cash-based but producers occasionally give soft credit to new bottlers or when launching a new product.

Key Bottlers in East Africa

[16] A.T. Kearney. (2015). *Retail in Africa: Still the next big thing.*

In Uganda and Tanzania, there exists an additional leg to the distribution fulfilment, that of a stockist. Unlike distributors, these are not loyal and stock competing products and other categories. In our view this presents somewhat of a risk. Whilst certain distributors are comfortable with this relationship – "ultimately the customer decides", we feel that it underplays the capacity for manufacturers and distributors to drive demand and creates potential holes in the feedback loop where new products are launched or when market pricing changes.

In our view the complexity of distribution makes it a key focus area for both existing and incumbent market participants. In Tanzania, *Bhakresa* and *MeTL*, two local players who have managed to gain a foothold in the industry in a short space of time, have leveraged their ability and experience in distributing other packaged goods. Both have significant market share in key local staples such as bread and edible oils and have essentially leveraged on their existing distribution infrastructure when expanding into soft drinks.

In the long term, there is sufficient evidence to suggest that numeric distribution will become easier, as more people move into cities, retail formalises and general logistic infrastructure improves. This however, remains some way off, whilst the opportunity to capture consumer throats remains very much in the present.

Coca-Cola Beverages Africa Distributor in Nairobi, Kenya

Stockist in Dar Es Salaam, Tanzania

SECTION 4:

Consumer trends in East Africa

We have observed trends in the beverages market in East Africa and find similarities with four global trends.

Packaging

Shift to PET results in a greater focus on sustainability

Context

Globally, there has been a shift from glass- packaged beverages to PET, largely driven by convenience. With this shift, multinationals have found themselves needing to look at the environmental impact of their production process and ensure a more deliberate focus on sustainability.

Global observation

Global Consumer Packaged Goods companies actively strategise and implement sustainable production methods and materials into their production process. In 2010, *PepsiCo* introduced eco- friendly packaging into the United States market by incorporating at least ten percent recycled PET back into their beverage production process.[17] *Nestle* has made a commitment to completely eliminate plastic straws and plans to launch one of their most popular brands, *Nesquik*, in new paper packaging towards the second half of 2019.[18]

The South African perspective

The shift to environmentally friendly packaging can also be observed in this market. In 2012 *The Coca- Cola Company* introduced their *Valpre "PlantBottle",* made from 30 percent plant- based materials and is 100 percent recyclable. The company also ensures that 45 thousand tons of PET bottles are diverted from landfills each year for reuse in the industry.

How it plays out in East Africa

In this market, sustainability looks different. As it stands, the recycling capability in East Africa has not yet reached the level of sophistication found in the global and South African markets. Uncontrolled landfills and dumping sites are a reality that is slowly being amended through governmental and private company partnerships. *The Coca- Cola Company* plans to implement a circular solution which will ensure it achieves its "World Without Waste" goal of collecting and recycling the equivalent of every bottle the company sells globally. The first country that has experienced this closed- loop circular economy in East Africa is Kenya in 2018.[19]

[17] Mother Nature Network. (2010, May 3). *Pepsi and the environment*. Retrieved from Mother Nature Network: httpps://www.mnn.com
[18] Nestlé. (2019). *What is Nestlé doing to tackle packaging waste.* Retrieved from Nestlé: https://www.nestle.com/ask-nestle/environment/answers/tackling-packaging-waste-plastic-bottles
[19] The Coca Cola Company. (2019, January 9). What if plastic never became waste? Retrieved from Coca Cola Africa: www.coca-colaafrica.com

Energy drinks

Health concerns to drive further sub- categorization

Origination of energy drinks

Energy tonic

Commercial energy

Cheap energy

Presently

Sophisticated energy

Energy drinks have been in existence for nearly 60 years. When first created, the purpose was to provide consumers with a natural boost of energy, and they were categorized primarily as a medicinal tonic drink and found primarily in healthcare stores and pharmacies.

Over time the function of energy drinks evolved. These beverages became commercialized and moved out of pharmacies and into major retail stores. This era of energy drinks introduced beverages such as Red Bull and Monster.

New players then entered the market and introduced affordability to the category and this resulted in cheap energy; an innovation on price which made energy drinks more accessible.

Now we see the category come full circle with sophisticated offerings that go beyond just offering an energy boost, but also offer neurological and physical benefits.

Context

Millennials are the largest consumers of energy drinks. They are driving the industry away from products with harmful and synthetic ingredients and shifting the focus to more natural and safe offerings.

In studying the global journey of energy drinks we find that in some countries, the function of the category has come full circle (from medicinal tonics to sophisticated that yield medicinal/ healing qualities), and more “naturally- enhanced” energy drinks are re-entering the market, causing further sub-categorization of the energy drink market. In contrast, most of the countries in Africa are still riding the wave of “cheap energy” with some markets like South Africa, playing with the reduction of sugar and more flavour offerings.

Global perspective

Increased concerns around the health impact of energy drinks have accelerated the fragmentation of the category globally. In the United States, although consumption of *Monster Energy* and *Red Bull* is still high, the number of consumers looking for more than just a simple energy source is increasing. As a result, new players like *MatchaBar and Bai Bubbles* are introducing sophisticated energy drinks which contain less sugar and more natural and organic ingredients that provide the caffeine kick consumers desire.

Unlike long- standing competitors, new entrants in the market provide products with extended performance that is not only safe but also contains ingredients which are neurologically beneficial and that can be used in multiple contexts such as the sports field, the gym, school or in the office.

The South African perspective

Although fragmentation in the energy drinks offering in South Africa does exist, the category distinctions in the mind of some consumers are still blurred. Energy drinks and sports drinks for example are viewed as substitutable as consumers continue to make purchasing decisions based on price and flavour or taste instead of functionality.

With health concerns around energy drinks, more sugar-free variants have entered the South African market. Companies like *Red Bull* have now introduced a sugar-free variant and retailers like *Dis-Chem* and *Woolworths* have become health- enthusiast havens, offering the consumer a wider energy drinks offering that consists of more naturally enhanced products such as *Scheckter’s organic energy*. With this said, the South African market still gravitates towards cheaper energy sources such as *Score, Mofaya* and *Dragon,* predominantly because most consumers in this market perceive energy drinks to be healthier, and the flavored variants as substitutes to carbonated soft drinks.

How it plays out in East Africa

The same behaviour in South Africa is observed in East Africa. With the low levels of household disposable income, consumers are easy targets for the cheapest energy drink that offers the highest sugar and caffeine content. Local players like *MeTL Group’s Mo Energy* in Tanzania and *Hariss International’s Rock Boom* in Uganda dominate this space, leveraging the familiarity and strength of their brands to cross-sell energy drinks at low price points. Much like the South African consumer, functional discernment is low at this stage, but we believe that the category will come full circle and replicate the American market as health and nutritional content discernment becomes a more critical topic to the East African market in the future.

Price

Local players to capture more of the soft drinks market through affordable pricing

Loading of Mo Energy in METL depo in Tanzania

Context

In analyzing this trend we have deduced that price is a much stronger trend in East Africa than it is globally. The affordability strategy is clear through local entrants in Africa whilst globally, market share growth is derived from product innovation when new players enter the market, as opposed to price.[20]

Global perspective

In the United States for example, sales have been driven more by product innovation and less by price. From a bottled water perspective, the increase in market fragmentation (as a result of new smaller player entering in the market) resulted in market share loss of the big players. This was driven by marketing, new flavours and functionality.

The South African perspective

Smaller players like Bevco, Kingsley and *Twizza* have begun capturing the lower income earners who for some time were not catered for from an affordability perspective. We predict that the market share of these new smaller market players will grow as they continue to improve the quality of their product offering and keep prices low.

How it plays out in East Africa

East Africa will continue to be a price-sensitive market to compete in due to low per capita incomes. Despite constrained disposable incomes, the demand for soft drinks will continue to rise and will be greatly attributable to the local players like *MeTL* and *Watercom* entering the market at much lower price points than long-standing market leaders. With their ability to serve the untouched lower income earners in remote geographical areas, whilst also converting the price-sensitive, middle- and upper-income earners, they have managed to grow market share over a short period of time and will continue to do so.

[20] Data derived from Euromonitor “Soft Drinks in the US” 2019 Country report

Health

Health- consciousness continues to influence purchasing decisions

Context

Growth in Health and Wellness is expected to come from Asia Pacific and the Middle East and Africa. With these two regions posting retail value growth of 3.3% and 4.2%, respectively.[21] Health is increasingly becoming a priority in global consumption preferences. In the past we have seen this through innovations in CSDs and energy drinks where competitors have introduced sugar- free variants as well as in in the alcoholic space with lite and alcohol-free subcategories.

Global perspective

Consumers are now pushing the boat out even further and demand is moving towards products perceived as more natural and healthier. Instead of reaching for sugar- free, low calorie products, consumers are now looking for “natural health” and less “synthetic health”. Products with short, recognizable ingredients lists which have little to no preservatives (such as *WTRMLN WTR* and *Health- Ade Kombucha*) will win the day. In this market, we should see a shift in consumption purchases which align to Organic, "Free From" and "Naturally Healthy" products.

The South African perspective

When observing the level of health- consciousness in this market, we find that South African consumers (those who are health conscious) are mature, as they go beyond company disclosure, conducting their own research and formulating their own perspectives on the health of products. Research has found that Instagram and online health blogs/ forums largely influence this market.[22]

How it plays out in East Africa

Healthy consumption decisions in East Africa, much like the rest of the world, have transcended to lifestyle choices. Although the spending power of consumers is low, they are still concerned about what they ingest. If a product is packaged, ingredient disclosure is very important to the East African consumer and they actively use this information to make smarter and healthier purchasing decisions. As a result of the complex value chain in East Africa, products with a short shelf- life (cold- pressed juices) are few and far between. In this market what works best and what exists in the environment is “synthetic health”. Competitors like *The Coca- Cola Company* and *Bakhresa Group* (operating in Tanzania) use terms such as “vitamin enriched” and “malt-extract” on their beverages to draw health conscious consumers. The market has not yet reached the point of providing truly wholesome, organic and natural beverages which also come with a steep price point that might not work in all areas in the region.

[21] Figures extracted from Euromonitor

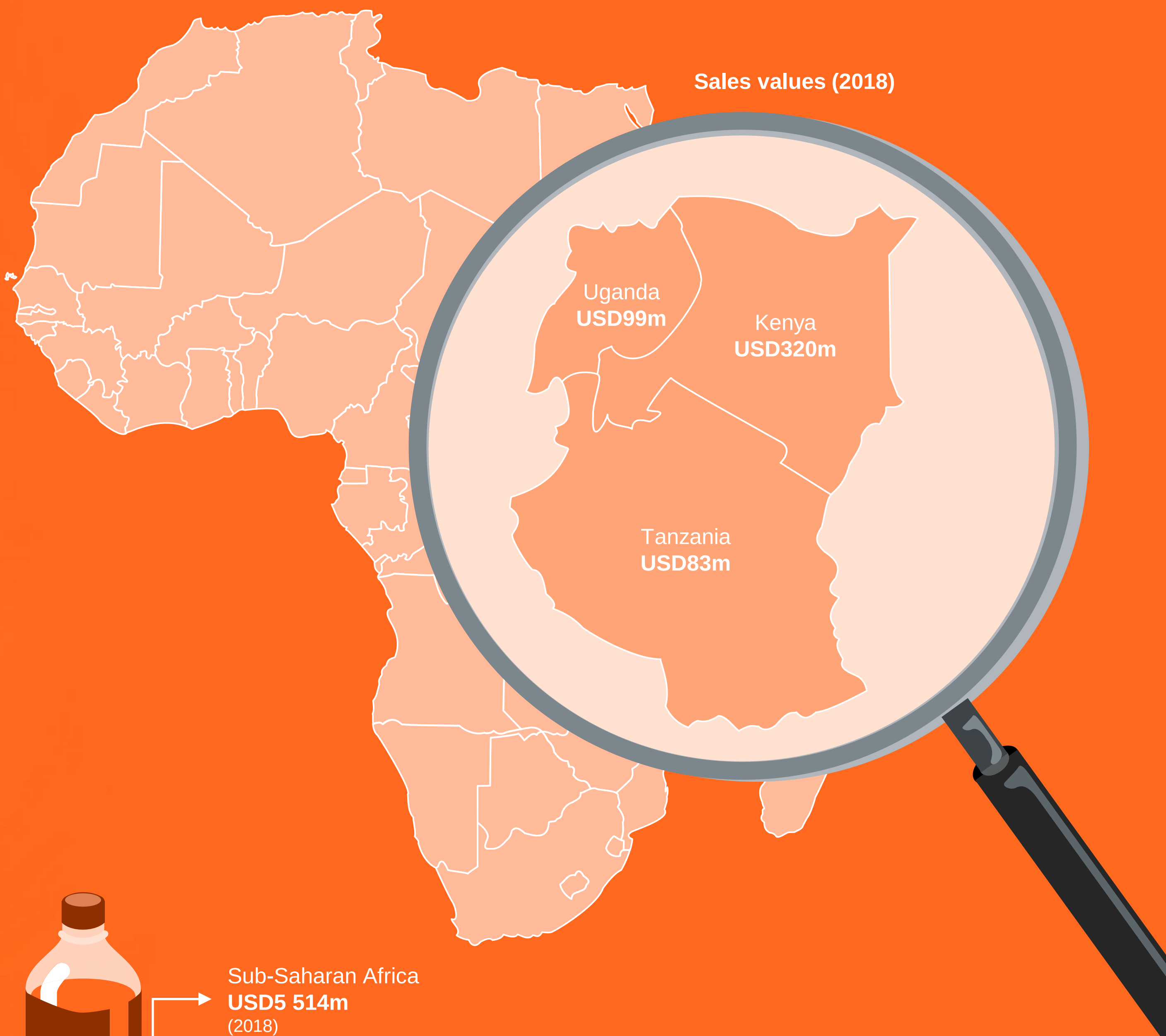
[22] Data derived from Euromonitor “Health and Wellness in South Africa” 2019 Country report

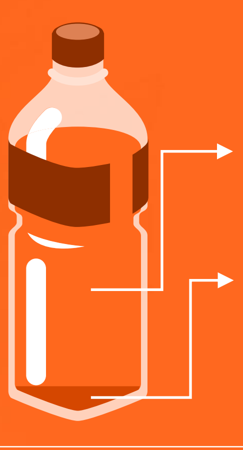
SECTION 5.1:

Soft Drink Categories

Carbonates in East Africa

Carbonates in East Africa[23]





Sub-Saharan Africa
USD5 514m
(2018)

East Africa
USD502m
(2018)

[23] All data sourced from BMI Research

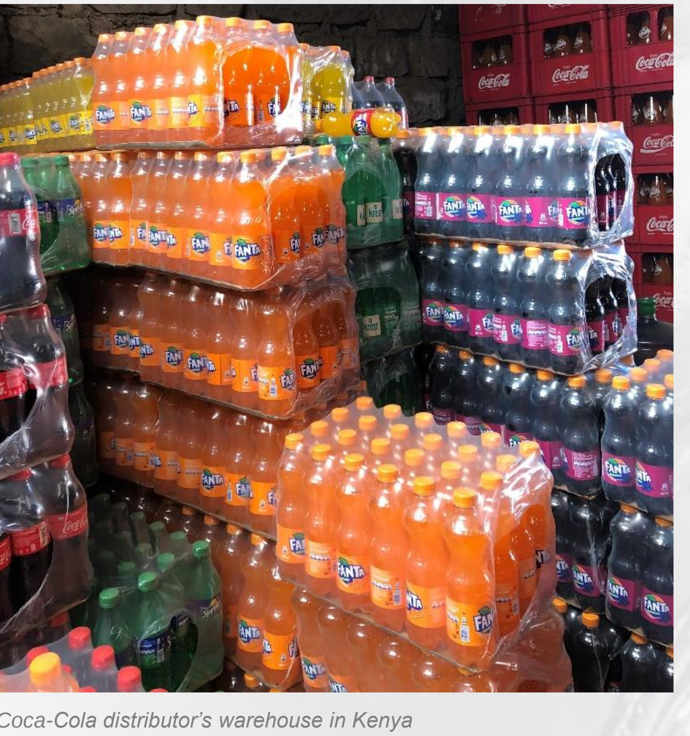
Carbonates category ranks as the largest soft drink category in East Africa.[24]

The category has been growing steadily due to its affordability, often cheaper than bottled water.

Competition– International players face strong local competition in all markets

The Coca-Cola Company is the leading company when it comes to carbonates across all three countries in East Africa. Its performance is attributed to its high-level advertising, which has led to higher brand awareness, and a well-established distribution network. It is more dominant in Kenya than in Uganda and Tanzania as *PepsiCo* does not have a significant presence in Kenya. Kenya also has an absence of well-established local firms in carbonates, unlike the likes of Uganda with *Hariss International* and Tanzania with *MeTL Group* and *Bakhresa Group*.

Carbonates found in modern retail stores in Kenya



Coca-Cola distributor's warehouse in Kenya

[24] All data sourced from BMI Research

Health-awareness among consumers is shifting consumers to “healthier” categories

There is a growing health awareness among consumers in East Africa, particularly in Kenya. This health awareness is causing consumers to shift into other categories such as juices that have positioned themselves as having a higher fruit content. Energy drinks are also perceived as healthier options. Millennials in particular, are starting to choose bottled water over carbonates, this is largely due to the influence of digital media.

As a result of these increasingly health-aware consumers, manufacturers have responded by introducing lower-sugar and naturally sweetened variants. *The Coca-Cola Company* launched a lemon-flavored carbonated drink, *Schweppes +C*, which targets a health-conscious consumer base in Kenya. The company has also launched *Coke Zero* in all three markets and *Fanta Zero* is being introduced in the Kenyan market later this year.

Disclosing nutritional content has also become a popular trend in this category as consumers are demanding to be more aware of what they are consuming.

Schweppes +C at Nairobi Bottlers office

Disclosure of nutritional content on Schweppes +C

Zip Zero in Shoprite Uganda

Fanta Zero at Nairobi bottler’s office

Disclosure of nutritional content on Fanta Zero

Coca-Cola Zero at Nairobi bottler’s office

Packaging – Shift from glass to PET

The Coca-Cola Company and *PepsiCo* have predominately sold their products in returnable glass bottles, but consumers are increasingly demanding more convenient packaging. Local players such as *Bidco Africa*, *Highlands Mineral Water Company*, *Bakhresa Group* and *MeTL Group* are stealing market share from the international players partially because they cater to this need of convenience. Consequently, *The Coca-Cola Company* and *PepsiCo* have also started producing more drinks in PET bottles.

Coca-Cola in a glass bottle in Kenya

Pepsi in glass bottles in Tanzania

Pack sizes – Seeing the introduction of smaller sizes

International players have responded to the issue of affordability by introducing smaller pack sizes to make their products more affordable to a wider audience of consumers.

Coca-Cola in smaller pack size in Kenya

Sprite in smaller pack size in Kenya

Flavours– Mango, Passion, Pineapple and Malt-based are the best-selling new flavours

The original cola and lemon flavours still dominate the market, however we also observed interesting new flavours across all three markets, including the mango flavour which is more popular in fruit juices, specifically in Kenya, but *The Coca-Cola Company* is in the process of introducing *Fanta Mango* to the market this year. *Fanta passion* is available across all three countries and *MeTL Group* and *Bakhresa Group* highlighted that passion and pineapple were among their best-selling flavours. Manufacturers also indicated that malt-based beverages were in their top three best-selling flavours. *The Coca-Cola Company* has its *Novida* brand, *Hariss International* has *Lavita* and *MeTL Group* and *Bakhresa Group* also have malt-based beverages.

Due to the issue of affordability, we believe local players will win market share in the short term. This is likely to push consumers towards these local companies with lower-priced carbonates offerings. In this context, we believe that international players are at a disadvantage to local players, which can offer similar drinks at much lower prices.

Fanta passion in Kenya

Fanta pineapple in Kenya

Mo passion in Tanzania

Lavita at a Shoprite in Uganda

Energy drinks in East Africa

Energy drinks in East Africa

Energy drinks are the fastest-growing soft drinks category in East Africa. In the past this category was reserved for the wealthier consumers, but now local companies have created value-oriented energy drinks to appeal to these previously neglected customers.

Competition – International players face strong local competition in all markets

More than any other brand, the modern energy drink category has been shaped by global market leader *Red Bull*. It was found across all three countries and was the first energy drink brand to be introduced to East Africa. *The Coca-Cola Company* has recently brought in *Power Play* and *Monster Energy* which are doing relatively well and have taken some market share from *Red Bull*. This is mainly due to the well-established distribution network the company has in the region. *PepsiCo* has a small presence in the category through its *Sting* brand.

In Uganda and Tanzania, more local players have entered this category and seem more appealing to the wider consumer base due to their affordable price points. Uganda's Riham's *Rock Boom* (which contributes a great portion of revenue for *Hariss International*) is by far the leading brand in the country. *Rock Boom* is half the price of *Red Bull*. In Tanzania, *Mo Energy* is the most popular energy drink, and this is mainly due to the fact that it is cheaper than the international brands and offers a bigger bottle size at the same price as the smaller bottles the other local players offer. *Red Bull* is sold at 3000 Tanzanian shillings whereas *Mo energy* is only 650 for a 400 ml bottle. *MeTL Group* has approximately 30 percent market share of energy drinks in the country. *Bakhresa Group's* best-selling product is also its energy drink. Other brands found in Tanzania include *Sayona Pawa, Vimto* and *Bullet.*

Packaging – Mainly PET but cans are also available

Most local players sell their products in PET bottles. *Red Bull* and *Monster* are however still mainly found in cans.

Various energy drinks players in Kenya

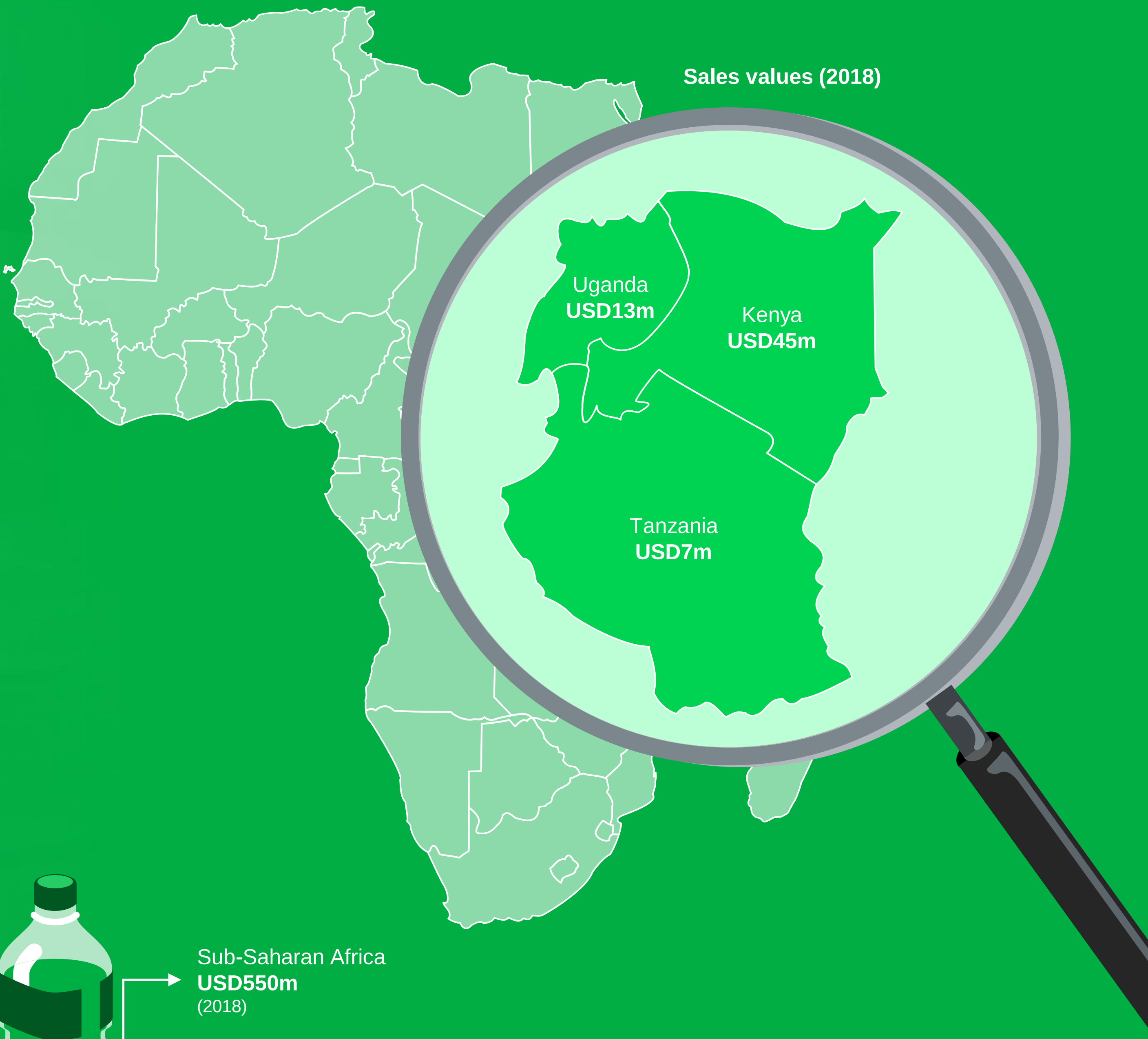
Monster Energy in cans in Kenya

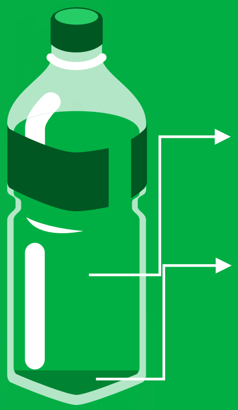
Riham's Rock Boom Energy drink in Uganda

Mo Energy and Azam Energy in PET bottles in Tanzania

Bottled Water in East Africa

Bottled Water in East Africa[25]





[25] All data sourced from Euromonitor and BMI Research

With the unreliable supply of safe drinking water,

still water in many parts of Africa continues to be consumed primarily as a commodity.

Competition – Fragmented market with many players and price sensitive consumers

Although *The Coca- Cola Company* has a market presence throughout East Africa, it is not the dominant player and is usually positioned as one of the four key players in the region. An example of this can be seen in Kenya where the dominant player in this category is *Aquamist*; Keringet (A *Coca- Cola* brand), comes in at 4th place in Kenya. Other strong players in this country are *Crown Foods Group* and *Highlands Mineral Water Company*. Uganda has more than 30 bottled water brands. Leading players include *Century Bottling Company,N.C. Beverages, Crown Beverages, Hariss International, Rwenzori Beverages and Aqua Coolers* which all share more than half of the bottled water market. In Tanzania, *Watercom* and *Cool Blue* stood out for their perceived high-quality offering.

With bottled water being a commodity in the region, it means that all consumers require access. The price sensitivity of consumers in this market results in a demand for the lowest priced water-leaving some victim to poor quality bottled water. The high consumer demand opened the market for many competitors to enter this space with relatively low barriers to entry from a manufacturing and regulatory perspective. Most local market entrants are predominantly CSD manufacturers looking to take the opportunity to diversify and produce affordable drinking water for consumers.

Shelf display of bottled water competitor brands in Uganda

Packaging – PET dominates the market

In East Africa more than 90 percent of bottled water packaging consists of PET. Due to the commodity nature of bottled water, in order to make their brand more accessible *The Coca- Cola Company* will start producing lower priced drinking water and in the near future (release date pending) *Dasani* will be packaged in glass returnable bottles that will be priced competitively.

PET bottled water found in formal and traditional markets in East Africa

Pack Sizes – Vary from on-the-go consumption to household use

Bottled water produced in this region comes in varying sizes. The standard drinking sizes of 350 millilitre and 600 millilitre are for on-the-go consumption with larger bottles for household use.

Pack sizes in the region vary from "on-the-go" to "household consumption"

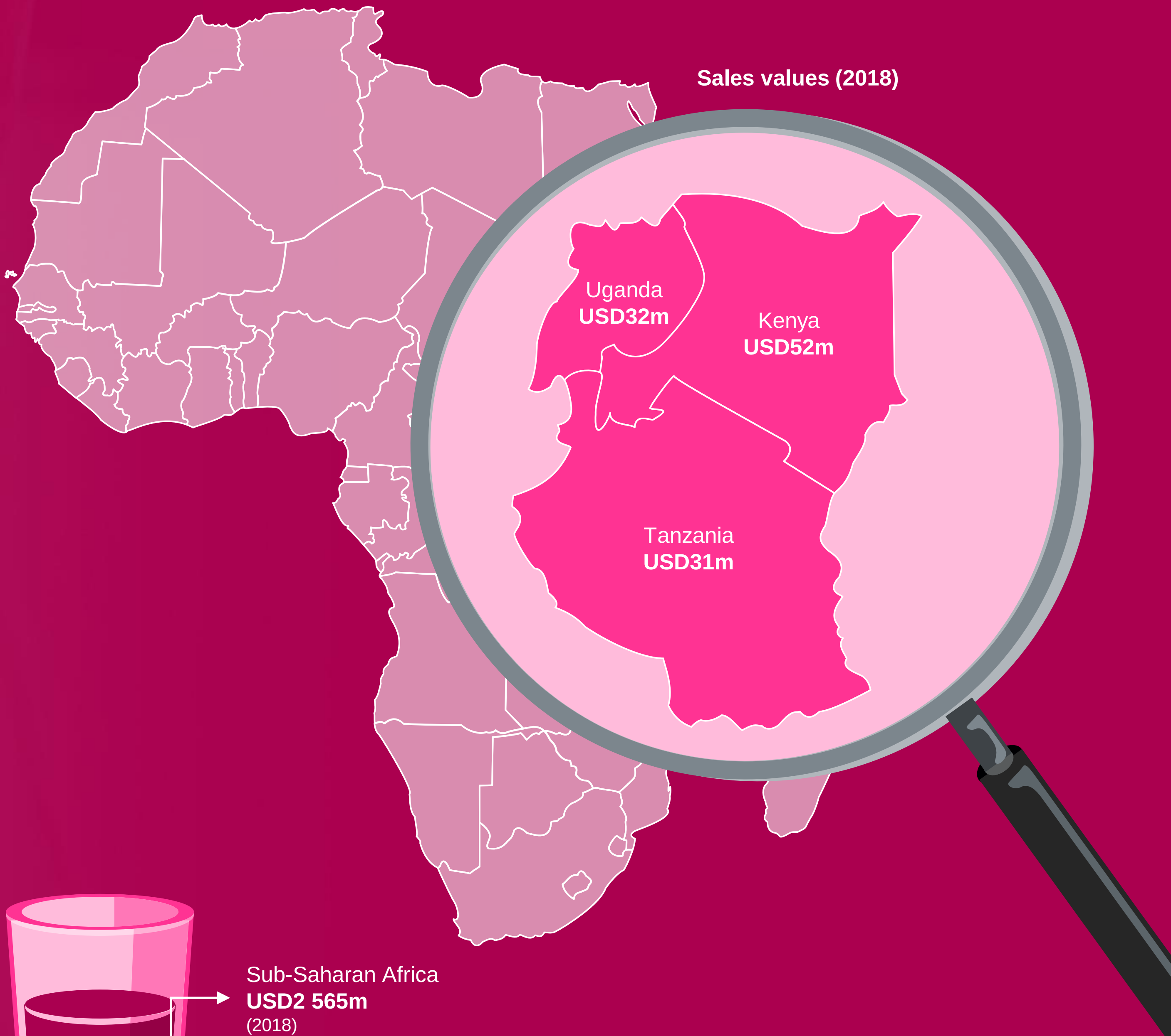
Flavours – Still water leads, sparkling water trails behind

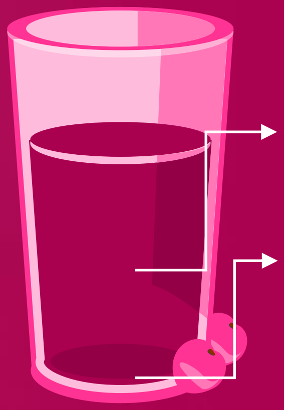
Although there is a presence of sparkling water on shelves, the greatest portion is found in upmarket retailers. In addition, the sentiment from competitors is that it is not a desirable category to enter at this stage as the market views it as an affluent product category.

Still and sparking Dasani water found in a retailer in Uganda

Juice Category in East Africa

Juice categories in East Africa [23]





[23] All data sourced from Euromonitor and BMI Research.

The juice category ranks as the third largest soft drinks category, behind CSDs and water.

Its growth outlook is favourable, thanks to a growing health awareness, coupled with a specific targeting of the youth population leading to expectations that it will continue to capture a greater share of consumer drink spend.

Competition – Coca-Cola Company faces strong local competition in all markets

From a regional perspective, *The Coca-Cola Company* is present in all markets with its *Minute Maid* brand holding the leading market share in Kenya[26] and arguably, across the region. The region benefits from a strong availability and cultivation of local fruits, which lends itself to local player participation. *Kevian Kenya*, through its *Afia* and *Pick n Peel* brands, holds sizeable markets shares in both Uganda and Kenya whilst *Sayona*, from the *Motisun Group* has made a strong entry into the Tanzanian market in recent years.

Interestingly, *PepsiCo* is absent from the category, which hampers its overall brand and ability to capture market share in the total beverage industry.

Health and the nag factor drive consumption

Several factors have led to the rise of juice consumption in the region, primarily among them, being an increasing awareness of health and a growing youth market. The rising number of middle-class households, many of whom are seeking healthier eating habits have shifted consumption towards juice.

Fifty-one percent of the regional population is under the age of 18[27] – this large cohort has presented brands with an opportunity to market to kids with smaller pack sizes, some reaching as small as 200 ml. In addition, many manufacturers are introducing resealable caps to reduce wastage where one serving is not consumed in one sitting.

Flavours – Single flavours dominate

Our research finds juice flavours centred around four main flavours – Mango, Orange, Pineapple and Guava to a lesser extent. Flavours are largely single, with *Excel Chemicals* (Kenya) recently introducing mixed flavours in its *FruitFull* brand. The most popular flavour varied by region but was strongly linked to perceptions about best local produce. Kenyans, for example, believed they produce the best mango in the region and accordingly, Mango is the best-selling juice flavour. A similar relationship exists between Ugandans and Pineapple. The Kenyan market had the greater spread of flavours.

[26] Euromonitor International. "Soft Drinks in Kenya." 2019.
[27] Economist Intelligence Unit. (2019, April).

Minute Maid a key brand across the region

Rresealable packs are increasingly popular

Formal retail channels carry a wide assortment of brands

SECTION 5.2:

Soft Drink Category Risks

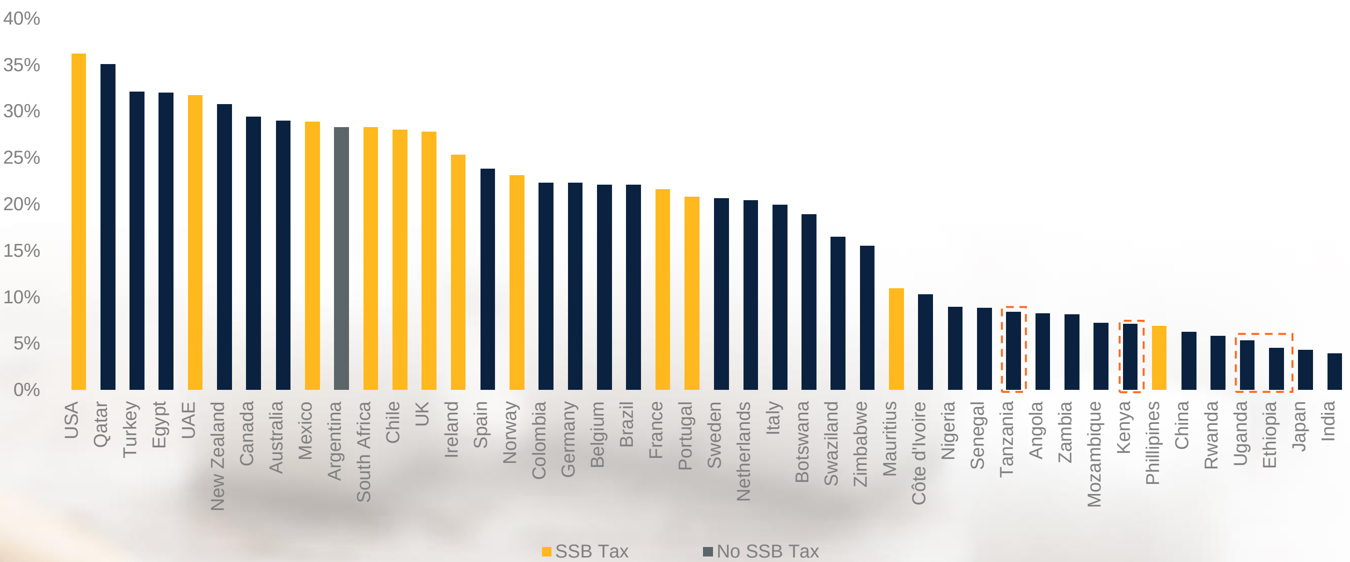
Sugary drink tax in East Africa – too soon?

Rising concerns around obesity, coupled with its economic impact has led to a swell in Sugar Sweetened Beverage (SSB) taxes around the world. In the past 24 months alone, the United Kingdom, Ireland, South Africa and Chile, among others have adopted SSB taxes. However, there remains conflicting views on the effectiveness of such taxes in combating obesity as both consumers and manufacturers differ in their responses to the tax.

We explore how SSB taxes have been implemented and how the industry has responded before opining on the likelihood of an SSB tax in East Africa.

In October 2016, the *World Health Organisation* reported that the prevalence of obesity had doubled between 1980 and 2014, with nearly half a billion people considered obese. It also raised concerns for childhood obesity, with 42 million classified as obese, a quarter of whom reside in Africa. *Mckinsey & Company* highlighted the costs of obesity stating "2 to 7 percent of all healthcare spending relates to measures to prevent and treat this condition, with up to 20 percent of all healthcare spending attributable to obesity, through related diseases such as Type 2 diabetes and heart disease".[28]

Obesity levels around the world



Source: Obesity ProCon

[28] Insitute of Economic Affairs. (2016). *Sugar Taxes: A briefing.*

In 2014, Mexico was the first major nation to implement a nationwide tax on sugar sweetened beverages with numerous countries following since.

Country	Implementation Date	Tax	Government Income	Impact	Market Reaction
Sri Lanka	November 2017	USD 0.17 cents per gram of sugar, reduced from USD 0.28 cents per gram	USD 28m	During Q1 2018 volume of beverage sales declined by 28% and by 40% in the third quarter of 2018	Ceylon Cold Stores , a unit of John Keells Holdings, saw earnings for the quarter ending December 31 2018 drop 32% to Rs.563.2 million
UK	April 2018	**Tiered**: >5g per 100ml - GBP18p per litre >8g per 100ml - GBP24p per litre	USD308m	In 2016, government predicted revenue of USD667m but has since revised down to USD308m as companies reformulated drinks in anticipation of the tax	While it is still early days, the impact of the soft drinks tax in Great Britain has so far been broadly in line with out expectations - CCEP CEO Damian Gammell
Ireland	May 2018	**Tiered** 5g-8g per 100ml - USD24c >8g per 100ml - USD36c	USD27m (1 April 2018 - 1 April 2019)	Raised €16.5m in first 6 months since implemented compared to a predicted €30m	"...We also know that our consumers want to manage their sugar intake, and this has driven our approach to reformulation and new product development" Mattieu Seguin Coca-Cola HBC Ireland
South Africa	April 2018	USD 0.15 cents per gram above 4 grams	USD 190m (1 April 2018 - 1 April 2019)	"We would have liked government to have imposed a 20% tax on sugary drinks to make a real impact on consumption.We also want to see the health department using the revenue from the levy to educate people about how to stay healthy."Sibongile Nkosi, Executive Director of the Healthy Living Alliance	"We had a reasonably good plan. I don't think we perhaps were as aggressive on the reformulations as we should have been. Competitors were more aggressive. And so we quickly course-corrected in the quarter and now we're better" - Coca Cola
Mexico	2014	1 peso per litre soda tax	21.4 billion pesos	Research carried out by health professionals indicated a pronounced impact, with household purchases of sugary drinks falling by an average of 7.6% y-o-y over the first two years of implementation.	Mexico's two largest bottlers of carbonated drinks , Coca-Cola FEMSA and Arca Continental, endured a challenging sales environment in 2014 but recovered sharply, with both companies achieving double-digit revenue growth in FY15 and FY16

Responses to the tax – Manufacturers

Manufacturers have largely pushed back on the implementations of SSB taxes, commenting on the potential impact on jobs and the larger value chain. Where it has been successfully implemented, they have responded by:

- By producing smaller pack sizes – In the UK neither *The Coca-Cola Company* or *PepsiCo.* changed the formula of their flagship cola's but instead sold smaller bottles at higher mark-ups.
- Reformulating – Manufacturers change the recipe of their soft drinks to reduce sugar levels to keep price increases minimal. In South Africa *The Coca-Cola Company* has reformulated several of their drinks.
- Seek alternative category acquisitions – The wave of sugar taxes has in part contributed to manufacturers seeking exposure to alternative categories, such as *PepsiCo's* acquisition of *Soda Stream* or *The Coca-Cola Company's* acquisition of *Costa Coffee.*

Responses to the tax – Consumers

Consumer response has rested largely on whether their demand is inelastic or not.

- In response to higher prices, consumers with inelastic demands shift expenditure around to accommodate price changes and keep consumption largely the same.
- Consumers respond to higher prices by switching to lower brands or even accessing the black market.
- Consumers reduce soft drink consumption, in line with the intention of the tax but buy high-calorie, high-sugar alternatives. In this instance, soft drink consumption is reduced but sugar intake remains largely the same.

Impact

In Mexico, one of the earliest to implement a SSB tax, consumption declined in the first two years following the tax but has since recovered from 2016. Growth has been supported not only by higher values but also increased volumes, which suggests consumers have overcome initial resistance to the higher prices. Furthermore, government revenue from the tax is on the increase, with the tax generating MXN21.4bn in 2015 from MXN18.3bn in 2014. This has led to calls for the tax to be doubled.

In South Africa, the SSB tax generated raised ZAR2.7bn in its first year and the tax was increased from 2.1c to 2.21c for every gram of sugar per 100 ml, with the first four grams exempt. Coca-Cola reported a 26 percent reduction in sugar across its range of sweetened beverages as it reformulated its portfolio. The sugar industry claimed that the tax had cost the industry nearly ZAR1 billion and 1 000 jobs as it relies heavily on the sugar demand of the soft drinks industry.[29]

East Africa next?

In our view, the current industry and consumer dynamic suggests that a sugar tax is not imminent.

The region has some of the lowest levels of obesity in the world, with Kenyan, Ugandan and Tanzanian levels all below 10 percent. As a measure to combat obesity alone, the low levels of obesity in the region suggest a sugar tax is unlikely, but the potential high level of obesity in the youth remains a risk.

The industry is currently characterised by two strong trends – downsizing in pack size and lower prices, both with a view of enticing price sensitive consumers. Reformulation that leads to even a slight price increase is likely to significantly alter market demand – potentially pushing consumers into a black market for soft drinks. Secondly, the current market has seen a strong downsizing trend, with 200-300 ml bottles among the fastest selling. We find it unlikely that manufacturers could consider even smaller sizes.

[29] Stainbank, G. (2019, March). *Sugar tax is a bitter pill - and there's no evidence it will curb obesity.* Retrieved from Fin24.

CARBONATED DRINKS

There is no legal obligation imposed on a manufacturer, packer or distributor of soft drinks to display nutritional information on the label of its products in East Africa.[30] However, since 2013 *The Coca-Cola Company*, as part of its business commitments to further contribute to healthier, happier and more active communities in the countries they operate in, are committed to providing transparent nutrition information, featuring calories on the front of all their packages.[31] Many local companies in the regions then followed suit in doing this.

In 2018 *The Coca-Cola Company* was taken to court by a consumer who claimed the company was discriminating against low-income consumers who were most likely to buy drinks in glass bottles, as the company did not disclose nutritional information on them. The judge argued that all consumers are equally entitled to access the information on the labels and therefore there was no justification for having the information on the plastic bottles only. *The Coca-Cola Company* is yet to implement this ruling.

No disclosure on glass bottles

Disclosure of nutritional content

[30] Kiplagat, S. (2018). Coca-Cola ordered to display nutrition data on glass bottles. Retrieved from https://www.nation.co.ke/business/Coca-Cola-display-nutrition-data-glass-bottles/996-4285486-130t86oz/index.html
[31] The Coca-Cola Company. (2013). Coca-Cola announces global commitments to help fight obesity. Retrieved from https://www.coca-colacompany.com/press-center/press-releases/coca-cola-announces-global-commitments-to-help-fight-obesity

ENERGY DRINKS

Disclosure of nutritional content on energy drinks

Globally, energy drink labels are unclear due to the lack of regulation. Many ingredients in energy drinks are "proprietary", and details are often not disclosed or may not be accurate. In the United States, it is up to the manufacturer to decide whether to list "nutrition facts" or "supplemental facts" on the label, and only benefits – not the potential harmful effects – are highlighted. Energy drinks can choose whether to be classified as conventional foods or dietary supplements hence the inconsistency in label disclosure.[32]

When observing the East African energy drinks market, we found that these drinks omit information to consumers in various clever ways of labelling. Some of these ways will be further explored below.

Misrepresentation of volumes consumed

According to food labelling regulations, the nutritive content of a foodstuff should be listed per 100 ml. The purpose of this regulation is to make it possible for the public to compare different products with a similar content by looking at the 100 ml column.[33] Energy drink manufacturers can decide whether to include the "Per Serving" column which is intended to show the consumer how much of each nutrient they will consume if they have a serving. Most global energy drink players disclose this information, however the disclosure was not found on some of the locally produced products. Most of the local brands are sold in large quantities of 300 ml and even 400 ml. So, if consumers check the nutritive content on the bottle they maybe misled into thinking that they have only had a third or a fourth of the caffeine and other ingredients, which is not true.

Warnings

Common additives to energy drinks – including taurine, creatine, guarana, glucuronolactone and B vitamins – add unpredictability to the mix.[34] Because these are not regulated, their effects are somewhat unknown. Even less is known about the effects of these additives when combined with caffeine, or when ingested by individuals of varying ages, health and body types. Some manufacturers do not even include the caffeine content per serving on their product labels, which adds to the unpredictability of their products' effects.

If new labelling requirements are imposed on energy drink manufacturers, including health warnings on caffeinated energy drinks, we predict the consumption of this category would decline. In our view, this category has experienced the most growth due to its benefits of consumption being oversold but hardly any disclosure on the potential side-effects of excessive caffeine, sugar and vitamin intakes.

Mo Energy disclosure

Kung Fu Energy disclosure

Red Bull disclosure

Power Play disclosure

Azam Energy disclosure

[30] Kiplagat, S. (2018). Coca-Cola ordered to display nutrition data on glass bottles. Retrieved from https://www.nation.co.ke/business/Coca-Cola-display-nutrition-data-glass-bottles/996-4285486-130t86oz/index.html
[31] The Coca-Cola Company. (2013). Coca-Cola announces global commitments to help fight obesity. Retrieved from https://www.coca-colacompany.com/press-center/press-releases/coca-cola-announces-global-commitments-to-help-fight-obesity
[32] Dennison, K (2013). Energy drink labels sometimes misleading. Retrieved from https://www.lhsfna.org/index.cfm/lifelines/november-2013/energy-drink-labels-sometimes-misleading/
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BOTTLED WATER

Bottled Water in East Africa: Under-regulated and fragmented

The current bottled water landscape presents itself as highly fragmented. The market is filled with numerous players and there is little to no regulation governing the manufacturing process of some brands in the region.

In this section we explore the regulatory landscape of Africa, the impact of counterfeit water and unregistered bottlers, and the possible economic benefits of a more regulated bottled water industry in East Africa.

The need for robust regulation

By definition, a regulated market is one which consists of government bodies and industry or labour groups who exert a level of oversight and control.[35] The regulation of bottled water, where it exists, is a very recent thing in Africa. Until 2006, bottled water in South Africa was broadly regulated according to the general safety and quality criteria governing the production of food. In 2006, through the counsel of South African Natural Bottled Water Association (SANBWA), the Department of Health drew up new legislation specific to the bottled water industry. The legislation is based on United Nations and World Health Organisation standards. Nigeria, the country accounting for half of the packaged water sales in Sub- Saharan Africa (USD305 million), is still being governed through an indirect legislation called the National Agency for Food and Drug Administration Control (NAFDAC).[36] It is the sole regulator established and empowered to enforce compliance with the drinking water qualities guideline values as recommended by the World Health Organization.

As it stands, Kenya has more than 350 players who are regulated by the *Kenya Bureau of Standards* (KEBS). In 2018, the bureau identified 157 water companies who had manufactured bottled water without a license. Some of these violations include companies operating from unknown locations, non-compliance to the requirements of the relevant water standards such as the code of hygiene, use of suspect water sources, as well as poor and misleading labelling. Majority of this uncertified water circulates in traditional retail channels.[37] In 2017 KEBS shut down the production of 5 brands which were found to have coliform bacteria as a result of faecal contamination and poor hygiene standards.[38]

The number of water bottlers operating in Uganda and Tanzania are unknown. Much like Kenya, Uganda battles with counterfeit water in the market and since inception, the industry has been operating unregulated until recently (in 2017). Tanzania has a bureau called the *Tanzania Bureau of Standards* (TBS) which oversees bottled water production in the country. Over the past ten years, the bureau has been fighting counterfeit water which has been released into the market with fake TBS accreditation logos.

As it stands, two of the three countries are governed by regulation. However, upon analysis what we find is that the regulation is new, not robust enough or inadequately enforced which results in the continuation of the counterfeit market. When comparing the KEBS water bottling legislation (which has the most advanced legislation of the three countries) with the South African Bureau of Standards (SABS), South Africa is quite advanced from a legislative perspective and thus both the economy and its people have been better off from this aspect.

How more stringent regulation can improve the East African economy

Packaged water in Africa has a dual functionality. It is primarily used as drinking water and secondly, households use it to feed their families and keep clean. In knowing this, there is no doubt that the demand for packaged water in Africa will continue to exist into the foreseeable future.

The biggest benefit that will arise from more stringent regulation is the protection of customers and the development of product trust. With an in-country bureau of standards backing the water quality of every produced bottle, the quality of water will increase, consumers will be protected and trust in bottled water will increase.

Another benefit of regulating the market is that it will reduce the level of fragmentation and enable competition as barriers to entry will increase. The policies and guidelines around manufacturing/ bottling will be outlined and enforced and those not willing/ able to compete will fall out of the competitive market for good reason (which is to protect consumers).

[35] Kenton, W. (2017, December 1). *Regulated Market.* Retrieved from Investopedia: https://www.investopedia.com/terms/r/regulated-market.asp
[36] Sourced from 2019 Euromonitor data
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SECTION 6:

Competitive Landscape

Global players – PepsiCo bottlers struggling to compete with The Coca-Cola Company bottlers

	The Coca-Cola Company	PepsiCo
Estimated East African market share	**~40%**	**~20%**
Main bottler	**Coca-Cola Beverages Africa**	**Continental Beverages** (7 UP Bottling Company)
Product portfolio		
Alcohol distribution?	Campari premium brands including: 	Not in East Africa
Investment in region	Plans to invest **USD100 million** in Kenya over the next 5 years to improve market penetration facilities	Invested **USD30 million** for a plant in Nairobi in 2013

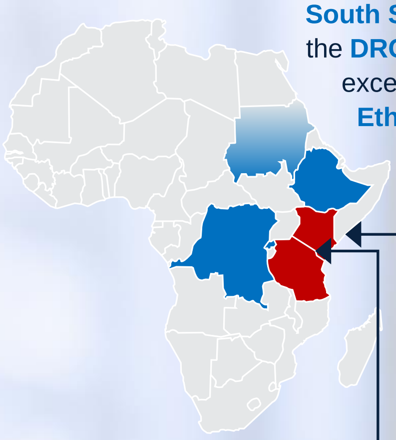
**Coca-Cola Beverages Africa (CCBA)* is the largest *Coca-Cola* bottling partner on the African continent. It shares the Kenyan market with one other independent bottler, *Coastal Bottlers*, which is also the only bottler to produce cans in the region. In Tanzania it shares the market with two independent bottlers that are owned by local investors.

*Crown Beverages (Pepsi bottler in Uganda) is owned by local investors.

East Africa focus markets

Focused on bigger markets such as **Kenya** and **Tanzania**

Focused on smaller countries in the region, holding strong market shares in **Rwanda, South Sudan** and the **DRC**. With the exception of **Ethiopia**.



The Coca-Cola Company's move to distribute alcoholic beverages

Crown Beverages (*CCBA* subsidiary) in Kenya signed an agreement with *Campari* in 2018 to distribute its premium alcohol brands.[39] *Rwenzori* (*CCBA* subsidiary) in Uganda also has a similar agreement to distribute *Distell* and *Campari's* alcoholic beverages. We find this an interesting move, and hints at some of the pressure *The Coca-Cola Company* is currently experiencing. Whilst sound in theory – *The Coca-Cola Company* currently supplies the same retailers, restaurants and bars that also require alcohol – implementation will not be straightforward. The nature of stock is fundamentally different to soft drinks, high value, low volume, changing many elements of the distribution chain. Our discussions with local alcoholic beverage players indicated that they expected it to struggle, at least initially.

The Coca-Cola Company's investment is paying off

The Coca-Cola Company's recent investment in the region to increase its product range and improve market penetration seems to be paying off, particularly in the region's biggest economy. *PepsiCo* re-entered the Kenyan market in 2011, after a four-decade absence.

Although *PepsiCo* maintained a presence in Tanzania and Uganda, being out of the country with the biggest economy is likely to have cost them from a brand position and revenue perspective. *PepsiCo* has focused on smaller countries in the region; restricted to its originals and lacks range in other categories outside of carbonates and it has not made as much investment into the region.

[39] Coca-Cola's Crown Beverages signs deal to distribute alcohol in Kenya. (2018). Retrieved from https://www.foodbusinessafrica.com/2018/07/12/coca-colas-crown-beverages-signs-deal-to-distribute-alcohol-in-kenya/

Homegrown companies on the rise across East Africa

	Aquamist	Kevian Kenya	Del Monte Kenya
Brief description	• One of the leading bottlers of bottled water in Kenya • It has recently diversified into juice blends and ice tea products	• Founded in 1992 • First product was “Mt Kenyan” bottled water • Producer of well-known Afia and Pick N’ Peel juice brands	• Controls significant share in Kenya’s juice market • Company supplies pineapple to USA entity
Countries	Kenya	Kenya	Kenya
Estimated country market share	12%	5%	-
Product portfolio			
Best-selling product			
Key developments	Menengai Oil Refineries agreed to acquire company. Competition Authority has approved transaction.	Kevian has unveiled plans of listing on Nairobi Securities Exchange	-
Ownership	Premji family	Kimani Rugendo	Fresh Del Monte Produce (USA)
Other considerations		• Company received funding from German financier DEG, of USD300 million which was for expansion into the malt business and the manufacturing of juice concentrate.	

MeTL Group	Bakhresa Group	Hariss International
• Company started producing water in 1997 then moved into other categories • Beverages contribute 5 percent to total group revenue	• Started in fruit juice and bottled water production before venturing into CSDs in 2011 • Beverages are sold under Azam brand • Contributes 65 percent to Bakhresa Food and Beverage	• 3rd largest manufacturer of soft drinks in Uganda • Entered beverage market in 2013 under the "Riham" brand • Target clientele are the price-sensitive mass market
Tanzania	Tanzania	Uganda
16%	**14%**	**12%**
		
 Mo energy drink	 Azam energy drink	 Rock Boom energy drink
-	-	-
Dewji family	Bakhresa family	Ahmad family
		• In 2013 Century Bottling of CCBA took Hariss to court on allegations of trademark infringement in relation to the production of the Riham Cola brand. • Riham drinks tend to be similar in names, flavours, packaging and pack size to that of Coca-Cola and Pepsi.

There are other new significant players that have entered the market such as *Sanoya* (under *Motisun Holdings*) which is becoming a fierce competitor in Tanzania. The Nyeri-based *Highlands Mineral Water* is the latest firm to venture into manufacturing soda, following in the footsteps of *Bidco Africa* and *Kevian* in Kenya.

The duopoly of US firms in the soft drinks industry in East Africa has been tested through competition with local entrants.

The entry of *Harris International* into Uganda, *Bakhresa Group* and *MeTL Group* into Tanzania as well as *Kevian Kenya* and others has shifted the industry that has been clearly dominated by the global giants. These local companies have a significant market share in their home countries with limited regional presence. However, many have indicated intentions of expanding into other neighbouring countries.

SECTION 7:

Opportunities

In this section we will look at where the opportunities lie in East Africa as well as the reasons why we believe they should be pursued.

The section blends opportunities with theory as well as brief case studies where other similar or like-minded investors and companies pursued the highlighted opportunity and reaped the benefits.

Opportunities in the market

Price innovation

Companies can either price at a premium or discount as a strategy for product differentiation. In East Africa, consumers are generally price sensitive thus companies adopt a discount pricing strategy.

Local players have created new, value-oriented soft drinks. In Uganda, *Hariss International* has beverages that are similar to that of *The Coca-Cola Company* and *PepsiCo* in flavour, packaging and pack sizes, but offered at significantly lower price points. As can be seen in the images Fanta 2l bottles are sold at 3800 Ugandan shillings versus 4200 for a 2l Mirinda versus 2900 for Hariss International's Funtime 2l. The same can be said for *MeTL Group* and *Bakhresa Group* that have made energy drinks more accessible to the wider market in Tanzania.

Hariss International's Funtime versus Fanta and Mirinda pricing

International players to take on "local"

The opportunity for international players is to roll out new local brands at significantly lower price points to restore market share from the regional or local brands and address price increases. It is similar to what *The Coca-Cola Company* tried to do with Sparletta in South Africa and Kinley in India.

Initially when Sparletta was launched in South Africa, it was significantly cheaper than the other Coca-Cola brands such as Coca-Cola and Fanta. The reason is that the product was created for the local market and was meant as a product offering to lower income consumers. With the increasing competition and introduction of other local brands that could be offered at cheaper prices, Sparletta has not been able to compete on their lower pricing, hence they are unable to capture the price-sensitive consumers.

In India, *The Coca-Cola Company* has developed a new value-based proposition for price-conscious consumers. The Kinley brand is expected to be up to 40 percent cheaper than the company's flagship brands, Coca-Cola, Sprite and Fanta.[40]

Non-consumption innovation

This is a circumstance where a majority of people in a society are unable to afford a particular product due to cost, time or skill constraints. This innovation transforms the existing complicated and expensive products to simple-to-use, more affordable products, thereby making them more accessible to a larger set of people in society, such as noodles in Nigeria.

When Haresh Aswani decided to start importing Indomie Noodles into Nigeria in 1988, Nigeria did not have an instant noodle market and the decks were stacked against his company, *Tolaram*. Nigeria was ruled by a military government, GDP per capita was only USD256, and 78 percent of people lived on less than USD2 per day. Tolaram entered Nigeria with a mission to target non-consumption. The company's vision was to bring affordability and quality to the lower socio-economic segments in the country. Since Tolaram began importing noodles into the country, it has built 11 factories that manufacture many of the inputs for the noodles. A packet of Indomie Noodles costs roughly USD18 cents, a product affordable by the majority of Nigerians. Tolaram has begun expansion plans into other African countries. Where many see obstacles, the company sees opportunity.[41]

Introduction of sports drinks and meal replacement beverages

If stricter regulations are imposed on the disclosure of nutritional information on energy drinks, we expect some of the more health-conscious consumers would no longer want to consume these products and therefore would be looking for a "healthier" alternative for an energy boost. Most sports drinks do not contain caffeine, they contain a moderate amount of mixed carbohydrates and contain sodium and other electrolyte minerals to replace those lost in sweat. Sports drinks offered at affordable price points, could therefore be a good substitute for consumers that are both health conscious and looking for that energy boost, particularly during sports.

With the increased awareness on health and the search for convenience, meal replacement beverages can satisfy both those requirements. These beverages can be consumed on-the-go as a "meal", they can speed up weight-loss results, many contain a variety of vitamins and minerals and they contain less calories than regular meals. Companies such as Coca-Cola Beverages Africa, have proven successful when launching their Minute Maid Fruity Boost drink which has added milk and minerals and is marketed as a meal supplement.

Minute Maid Fruity Boost in Kenya

[40] Coca-Cola takes on 'B-brands'. (2017). Retrieved from https://www.warc.com/newsandopinion/news/cocacola_takes_on_b_brands/38953
[41] Ojomo, E. How one company defied the odds and is grossing almost $1 billion in revenue… in Nigeria. Retrieved from https://sheleadsafrica.org/how-one-company-defied-the-odds/

Category Innovation

In the past companies have entered new markets by introducing new sub-categories with slight variances on existing products. In Kenya, Uganda and Tanzania, this has been especially true with the introduction of beverages primarily aimed at health-conscious consumers.

"Zero Beer" to diversify product range and capture health- conscious consumers

In the current market, this category innovation has presented itself through companies such as *Diageo* with the introduction of reduced- alcohol/ lite beer such as *Tusker* in Kenya and *Serengeti Lager* in Tanzania. In following the "health- conscious" trend and comparing it to what is taking place globally, we believe that an opportunity exists for competitors to introduce "zero beer" into their product lines.

Zero beer has historically displayed a higher growth rate than normal beer and targets a new type of consumer looking for a healthy alternative. Another advantage of the product is that it has the potential to capture both alcoholic (beer predominantly) and non- alcoholic consumers. With *Coca- Cola Beverages Africa* venturing into the supply of both soft and alcoholic drinks, this would be a natural and fitting category to introduce into their product line.

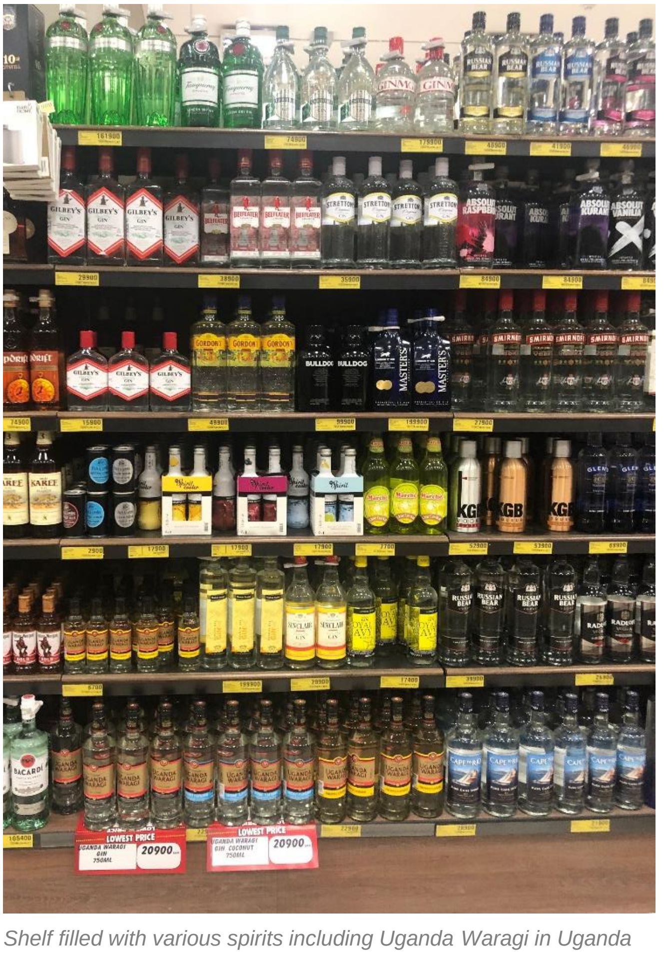
According to the *European Centre for Monitoring Alcohol Marketing (EUCAM)*, the global growth of beer is being impacted by an increased focus on health and well-being.[42] In 2016, AB InBev launched their "Castle Free" beer, followed by *Heineken in* 2018. This is a category that *Bavaria* and *Diageo* have dominated globally. Since 1999, Non- alcoholic beers have been growing at a CAGR of more than 3.5% which is higher than the forecasted beer growth in the foreseeable future.[43]

Diversify product lines with flavour variants

Flavour is a very important decision-making factor in East Africa. This has been proven true when *Diageo* successfully introduced a pineapple- flavoured spirit through their *Uganda Waragi* offering. A possible reason why mango and pineapple have a high consumption preference in this region is because both these fruit are familiar to the locals. Mangoes grow in abundance in Kenya, and Uganda has gained a reputation for cultivating the sweetest pineapples in the region and worldwide.

With the growing number of energy drink consumers in East Africa, the introduction of flavoured- energy drinks could prove favourable. *Red Bull* introduced their flavoured range in the United Kingdom which consists of "Orange" and "Tropical fruits" sugar- free variants. With mango and pineapple being so popular In East Africa, the introduction of these flavours in energy drinks could be a great opportunity. Flavoured water could also prove a favourable category to introduce for the health- conscious consumers in the region who still wants something sweet but "more natural" and healthy.

Store display of reduced alcohol beer in Uganda



Shelf filled with various spirits including Uganda Waragi in Uganda

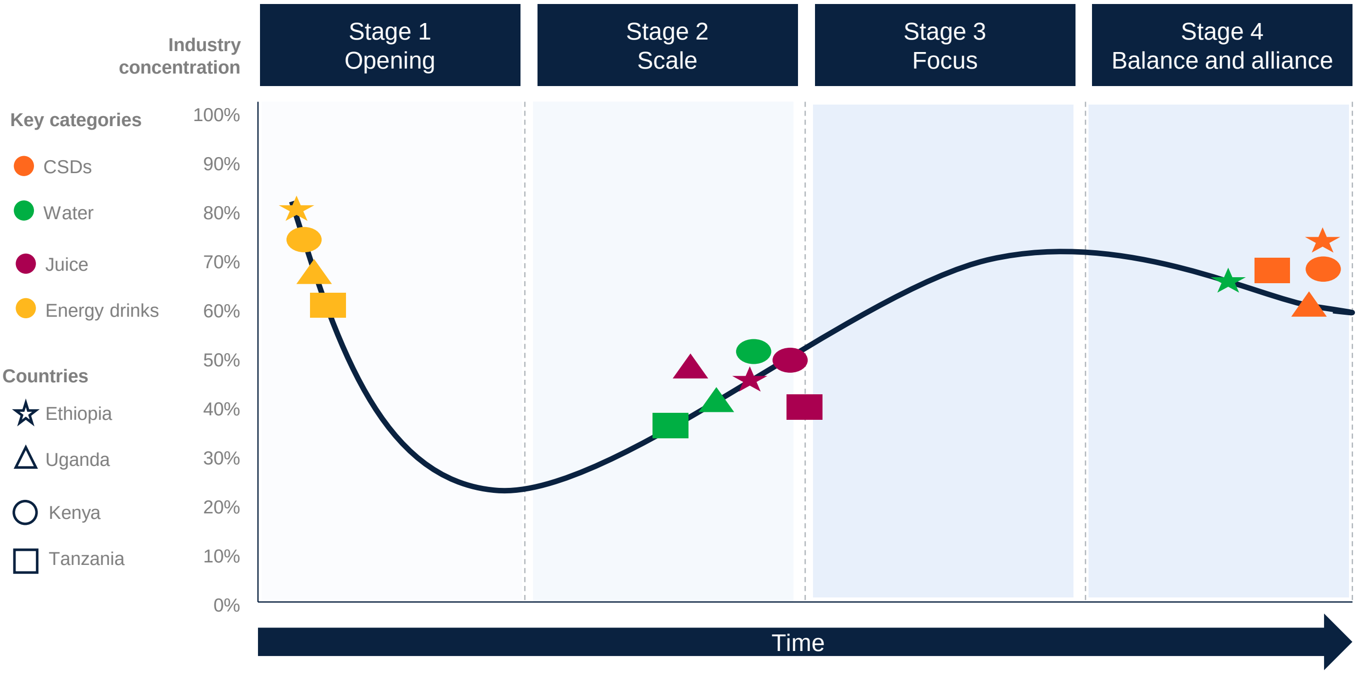
[42] European Centre for Monitoring Alcohol Marketing. (2018, February 18). *Growth in the alcohol- free beer market: A threat to soft drinks or ordinary beer?* Retrieved from eucam.info: www.eucam.info

[43] Arthur, R. (2018, June 5). *The key trend in the global beer industry? "Drinking less but drinking better".* Retrieved from Beverage Daily: https://www.beveragedaily.com/Article/2018/06/05/Drinking-less-but-drinking-better-Key-trends-in-the-global-beer-industry?utm_source=copyright&utm_medium=OnSite&utm_campaign=copyright

Room to consolidate?

Recent research suggests that new industries follow a predictable consolidation path from early fragmentation to matured consolidation . understanding the stages of the life cycle, and where an industry currently sits, is a key strategic understanding for both existing companies and potential investors. Arguably, each category within each country is at a different stage in the life cycle[44].

Stages of Consolidation



Source: Harvard Business Review

Stage 1 - Opening

In the opening stage of the consolidation life cycle, new market products hold a near 100 percent market share but it soon erodes as competitors launch competing products. We see this relationship most clearly with energy drinks in East Africa. *Red Bull* was the first to introduce consumers to energy drinks which quickly gained traction owing to its taste and energy content. Once proved, competitors quickly launched similar products, capitalising on the shortcomings of *Red Bull* – a high price point and limited distribution. Local players in Uganda and Tanzania have been most successful in disrupting its initial dominance.

Stage 2 - Scale

The second stage of consolidation is characterised by companies' building scale, brand awareness and competitive uniqueness. In East Africa, brand awareness and scale are key focus areas in driving lower price points. During this stage the market is at its most saturated with brands competing for a share of consumer wallets. Relatively low barriers to entry and high visibility of market growth have pushed many consumer companies into this space. We believe that the juice and water categories in East Africa are in this stage in the consolidation life cycle.

Stage 3 – Focus

The third stage of consolidation factors into account the reality that markets cannot sustain too many competitors, especially in a market that has priced down so significantly. Successful companies' bed down their offering and often use this position to acquire competing brands. We don't believe any category is currently in this stage – the industry has not seen large scale acquisitions, nor is their specific focus on underlying profitability

[44] Graeme K Deans, F. K. (2002). Harvard Business Review.

Stage 4 – Balance and Alliance

In the fourth and final stage of industry consolidation, two to three players maintain around 80 percent of the market, with strong defensibility. Further consolidation is unlikely because companies are recognised competitors of a similar size and would likely not receive competition approval. Carbonated soft drinks in Kenya are a prime example of a category in the fourth stage. *The Coca-Cola Company*, through its core bottler, *Coca-Cola Beverages Africa*, has leveraged a 70-year history in the country and outlasted market exits and re-entries from PepsiCo. Many of the local companies we spoke to have had to fight a “Coke buyout” which aimed to strengthen its market position and limit competition. In recent years it has come under pressure as smaller, nimbler players target CSDs which has arguably seen it lose some market share.
In our opinion, the juice category holds more potential for future consolidation than water.

No single player dominates the juice category in any country, with three to four players holding similar market shares. With the ability to source locally and export across the region as regulation improves, there exists an opportunity to consolidate key bottlers and access 120 million people with a growing affinity to juices.

CONCLUSION

The East African Beverage landscape is a work- in progress and sparking in the foreseeable future.

When conducting these primary research pieces, our aim has always been to live the work we do. Desktop research can only take you so far, hence why in-country visits are so crucial. Nothing brings consumer trends to life better than a real-world trade visit. When the team set out on this project, our primary goal was to ascertain whether the East African soft drinks landscape (Kenya, Uganda and Tanzania) was one which was worth investor attention.

It comes with no doubt that the operating landscape on the African continent comes with challenges that many other continents have overcome or learned to manage more efficiently overtime. The East Africa Community, which has been addressed in the report, is evidence of the amount of progress that still needs to be made in order to ensure that intra and inter- regional trade is effective.

Another point to note is the vast difference that can be found within a single region and country. Time taken to understand the consumer behaviour and how it translates or influences various economies will prove most beneficial.

The one thing that stands out most in this report on the East African region observed, is the strong prevalence and large market share of local companies. These companies have been observed to play on their local advantage of low manufacturing costs and governmental backing in order to penetrate the market successfully and reach a mass consumer following by leveraging on the accessibility factor of their products.

This is not to say that multinationals will be at a disadvantage though. We have observed that with the adoption of a long- term approach, many global multinationals have attained rewarding returns from the continent, with some generating more than half of their revenue from countries in the African regions. However these companies also took the time to understand their operating environment and form strong local partnerships so as to work alongside the in-country governments in mutually- beneficial relationships.

We hope that this report and those that follow will drive an understanding of African countries and regions beyond their macroeconomic variables. We believe that the African continent is positioned for growth and the horizon is in fact ‘sparkling and not still’.

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