

Virginia ABC Overview of Operations

Senate Finance and Appropriations Public Safety Subcommittee
January 26, 2022

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Virginia Alcoholic Beverage Control Authority

During 2018 Virginia ABC transitioned from a Department to an Authority

- Continuing to function as a market participant and regulator
 - Sole distributor and retailer of spirits
 - Regulate three tiers of alcoholic beverage industry

ABC Authority Accomplishments

- Procured IT services entirely outside of VITA while modernizing IT systems
- Reform and streamlining of ABC license structure
- Implemented Summary Suspension process to take action against licensees posing continuing threats to public safety
- Obtained reaccreditation by Virginia Law Enforcement Professional Standards Commission
- Named Overall Winner for 2021 *StateWays* Best Practices Awards - “Best Control State”
- Named to Beverage Dynamics Top 100 Retailers – 2020 and 2021
- Named Alcohol Law Enforcement Agency of the Year in 2021 and 2018 by National Liquor Law Enforcement Association
- Utilized “turn key” procurement process to build and operate a new \$100M central office and distribution center
- Maintained operations during the pandemic through personnel and compensation actions available as an authority
- Provided regulatory guidance and support allowing licensed businesses to continue to operate during the pandemic



Current State of the Control State

- **Mission Critical Statistics**
 - FY 2021 Gross Sales of \$1,355 million (up 13.5%)
 - FY 2021 Profits of \$237 million (up 11.9%)
 - Retail Licenses: 20,148 (down from 20,204)
 - Total Cases shipped to ABC stores: 6,305,184 (up 7.6%)
- **Operating Expense**
 - FY 2021: \$901.7 million (up 14.7%)
 - FY 2021 Operating expenses include: alcohol – 71.3%, personnel – 16.4%, retail occupancy - 4.3% and contractual (VITA, freight) – 6.3%
- **Employee Numbers**
 - At end of FY 2021 ABC had 4,813 total employees
 - 1,299 full-time employees
 - 3,514 part-time employees

Virginia ABC's 2021 Revenue Recipe

\$1.4 BILLION TOTAL REVENUE!

Did you know?

If Virginia were to replace the millions of dollars generated by Virginia ABC, each taxpayer would need to pay another \$151 in taxes.

\$616.4M transferred to the Commonwealth's General Fund

\$237.3M

Sales Profit

\$294M

Retail Taxes

\$85.1M

Wine/Beer Taxes



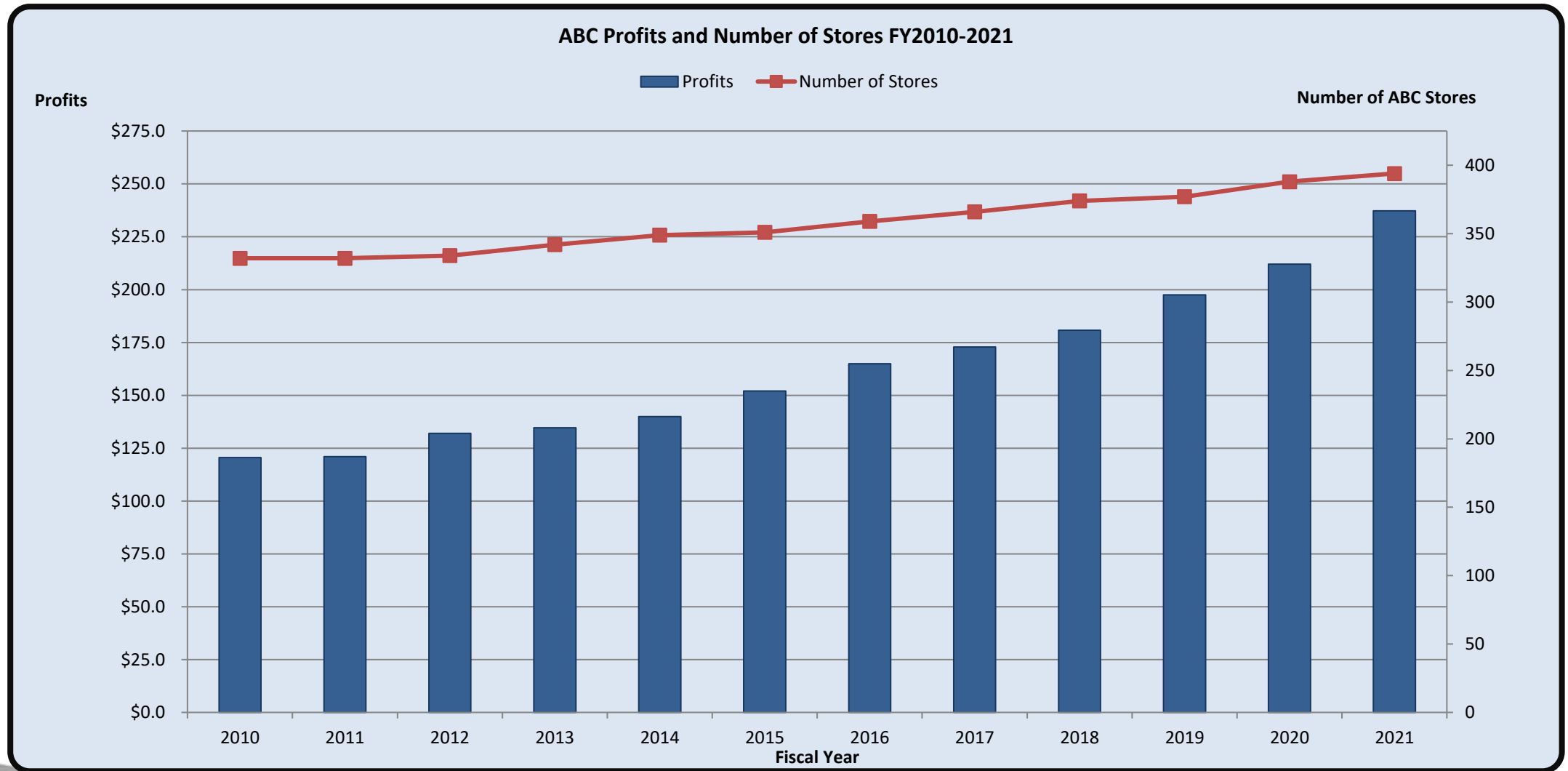
Where does the General Fund go?

Education	(42.0%)
Health & Human Resources	(32.5%)
General Government	(10.1%)
Public Safety	(9.6%)
Other	(5.8%)

How does Virginia ABC benefit you?



Historical Profit Growth



Contributions to Commonwealth Last 7 Years Total \$3.4B

FY 2021 increased \$71 million over FY 2020, \$207 million over FY 2015

Dollars in Millions

Revenue Source	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021
ABC profit transfers	\$152.0	\$164.9	\$171.2	\$180.8	\$196.7	\$212.1	\$237.3
State excise taxes	\$139.8	\$147.8	\$154.4	\$161.5	\$174.1	\$193.7	\$220.1
General sales tax	\$39.2	\$41.3	\$43.3	\$45.4	\$48.8	\$57.7	\$73.9
Wine liter tax	\$35.2	\$36.2	\$36.8	\$38.2	\$38.5	\$39.6	\$42.0
Malt beverage tax	\$42.9	\$43.2	\$42.8	\$42.9	\$41.4	\$42.2	\$43.1
Total	\$409.3	\$433.4	\$448.6	\$467.2	\$499.5	\$545.3	\$616.4

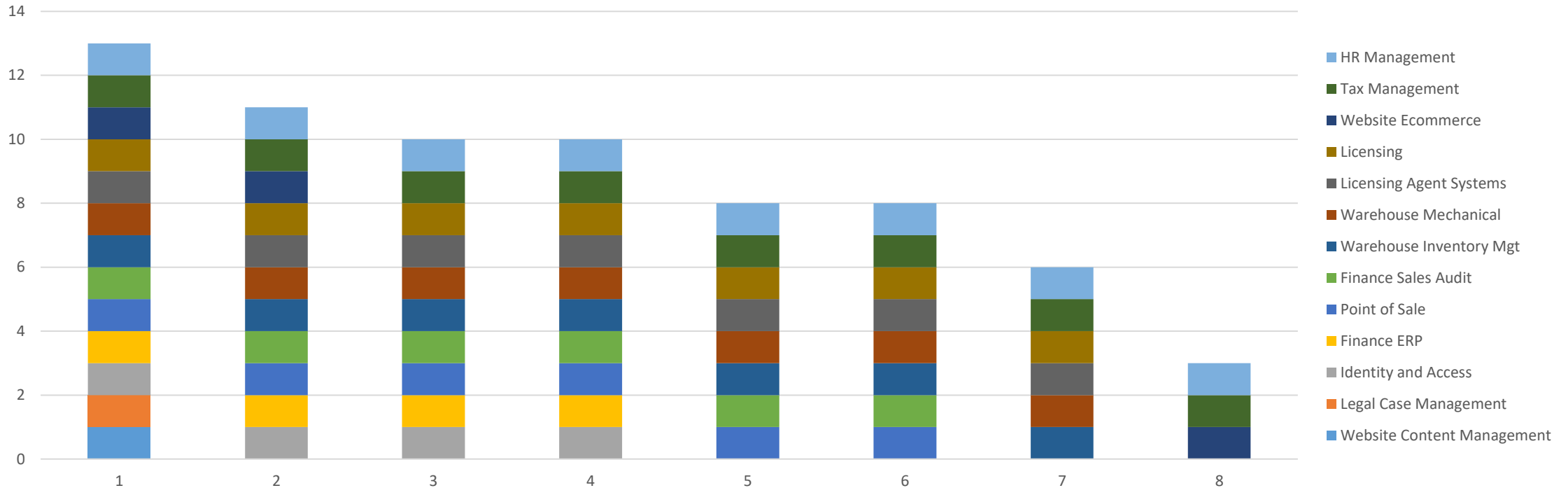
ABC IT Modernization

- Assessment conducted as part of a 2014 review of ABC's Operations determined aging IT infrastructure threatened operations and revenue generation
- We have made huge progress in major systems modernization. Most of ABC systems are current or have active projects planned to become current.
 - Completed projects
 - Financial System Replacement – FY19
 - Web Redesign 1.0 – FY15
 - Point of Sale/Sales Audit – FY21
 - ABC Domain and Network rebuild FY21
 - Migration to Cloud / From CESC (and off VITA services) FY21&22
 - Warehouse replacement – FY22
 - Licensing - FY22
 - Pending projects
 - HR Information System – approved 2021 legislative session starts FY23
 - Customer Support and Ticketing - FY22/23
 - Web Redesign/eCommerce Program 2.0 FY22 - 24
 - Tax Management FY23 planned
- New paradigm is to keep systems current, rather than run beyond end of life. With SaaS solutions being preferred



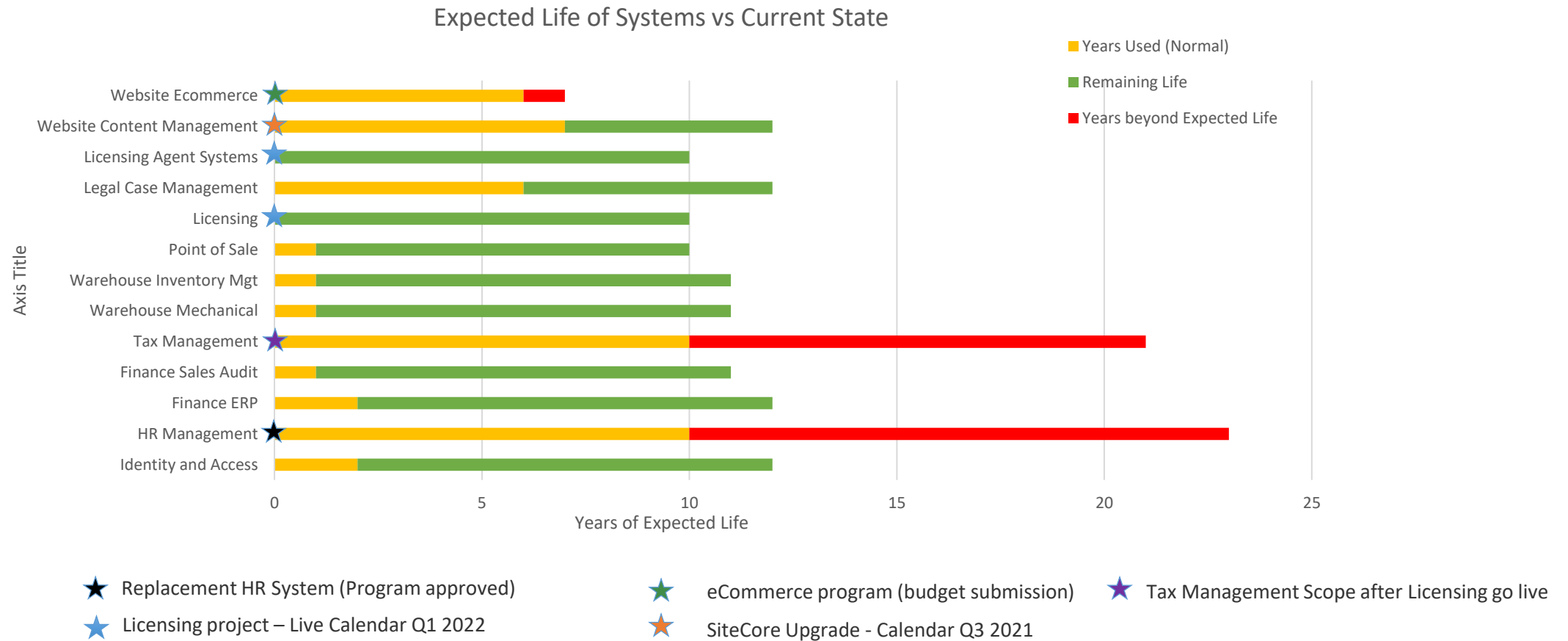
In 2014 ABC's technical debt was huge. Almost every system was beyond its useful life and or obsolete and unsupported

Number of ABC systems in use beyond their expected life by year



Although only 3 major business functions are beyond end of life, each is composed of multiple parts – HR is 5 systems, Tax Management - 3 systems and eCommerce modernization requires change to most retail and logistics systems

Expected Life of ABC Systems Compared to Current System State



eCommerce was the first 'next generation' system for ABC, built as custom software in 2015 on top of SiteCore, it has become a bottleneck to our capability to expand Omnichannel sales.

Licensing and Enforcement

- Bureau of Law Enforcement
 - 110 employees
 - 88 sworn agents in 9 field offices
 - Field agents focus on retail and banquet license investigations
 - Compliance agents handle wholesale and manufacturer licenses
 - 22 civilian staff in Licensing and Records Management
 - 20,148 retail licensees
 - 24,000 one-day banquet licenses
 - Activities include site inspections, application investigations, covert observations, planned operations and criminal investigations
 - Tax Management responsible for \$80M in excise tax collections
- Hearings Division
 - Adjudicates almost 375 cases annually (average over the past 3 years)
 - Most frequent cases involved underage sales and mixed beverage ratio (§4.1-114)
 - Reforms made as part of Authority transition
 - Average turnaround time for all cases from date received in Hearings to disposition for the past 3 years is 107 days (COVID-19 caused a delay due to work from home orders). Prior to COVID-19 the average turnaround time was 50 days.
 - \$2,056,289.27 in civil penalties collected from 2019 to date.

Enforcement Activities



License System
Implementation



License Reform

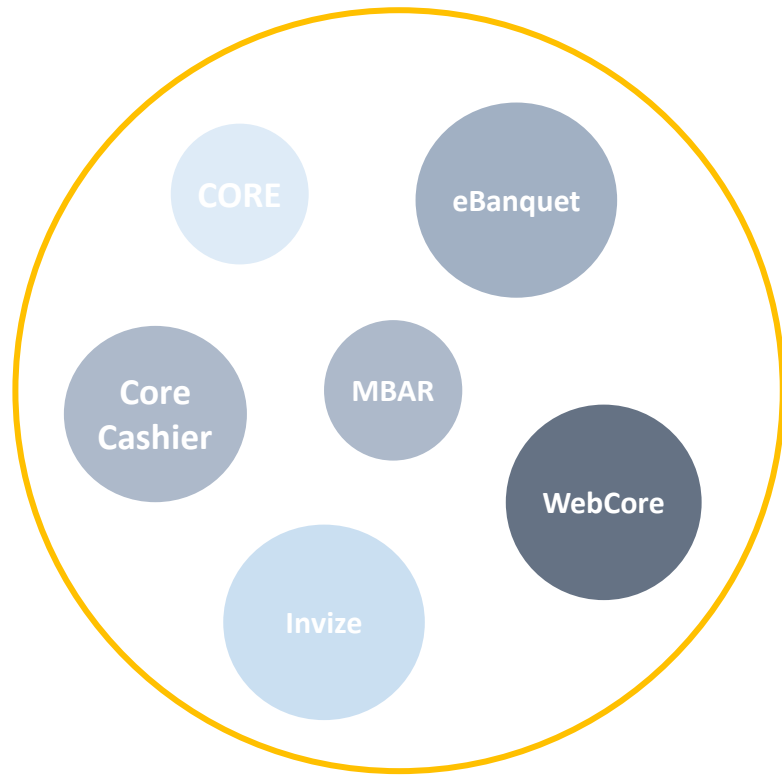


Direct Shipping



Public Safety Cases

Moving away from a paper driven process ensures a more consistent application experience, visibility into application status, and create a foundation for future upgrades.



- Current state, entire licensing process; application, renewal, and hearings are paper-driven
- The new licensing system will replace 6 different internal facing applications currently used by Virginia ABC: Core, CoreCashier, Webcore, MBAR, eBanquet, and Invize.
- Most of these applications were “home-grown”, highly customized, but now use obsolete technology, creating significant risk to the Authority.
- Currently, no public facing online interaction with licensees (except e Banquet). Entire licensing process; application, renewal, hearings are paper-driven.

Shared benefits for licensees and Virginia ABC

Why a web-based platform is key to our success



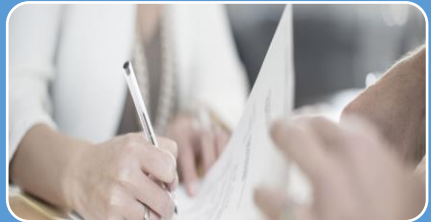
Convenience for Licensees and Businesses

- Available 24/7 whenever and wherever you are
- Greater flexibility for primary business
- Real time accessibility to materials and license information
- Works from your computer or mobile devices



Virginia ABC Benefits

- Promotes consistency across similarly situated businesses
- Provides a streamlined process for issuing licenses for a wide spectrum of businesses
- Reduces manual process and improves visibility



Perform Business Transactions

- Applications – renewals, modification, surrenders, etc.
- Financial Transactions – payment of all fees, fines, taxes, etc.
- Hearings and Appeals – reporting and correspondence
- Training Records – officially record responsibility training such as RSVP and MART



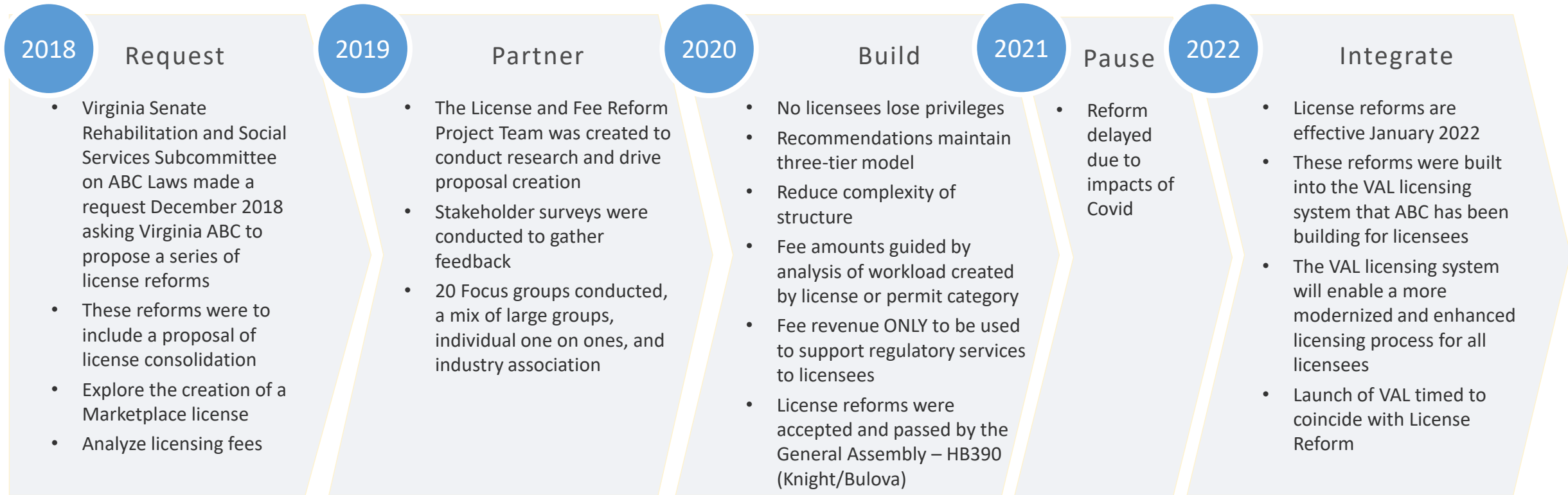
New Licensing and Fee Structure

- Consolidates 152 existing licenses down to 71 in a set of 12 categories
- Reduces complexity and duplicative processes for licensees

License Reform



We took a holistic approach to License Reform and partnered with licensees at every stage. The effort produced a comprehensive reform package that reflected the priorities of both licensees and the Commonwealth of Virginia.



Comprehensive license reform allowed Virginia ABC to consolidate, restructure and standardize licenses to enable efficiencies for our customers.

Benefits to Licensees

- Greater flexibility for primary business
- Real time accessibility to application materials and license information

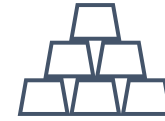
Benefits to Virginia ABC

- Consistency across similarly situated businesses
- A streamlined process for issuing licenses for a wide spectrum of businesses



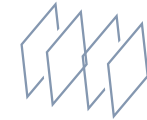
Consolidate

- Reduced number of licenses by more than 50%
- Mixed Beverage License — combines separate licenses for wine and beer includes wine and beer on and off premises
- Marketplace License — combines specialty licenses under one umbrella license



Restructure

- Expanded seating capacity tiers
- Previous Retail On-Premises licenses now include on-and-off premises (Off premises applies to wine and beer)



Standardize

- Most Mixed beverages licenses now include wine and beer on-and-off premises (formally just on-premises)
- No longer just an on-premise beer license; license includes both wine and beer
- Consistent sample/tasting serving sizes
- Keg, delivery, and tasting privileges included for all Retail Off-premises licenses

DTC Enforcement and Compliance Efforts

- DTC Wine Shipping in 2020 grew to \$3.7B, a 27% increase
- Virginia ABC is partnering with the Virginia authorized common carriers to stop unlicensed shippers shipping into Virginia
 - Illegal shipping is responsible for loss of revenue to Virginia through excise taxes and sales taxes not being collected
- Virginia is in top 10 of direct to consumer shipping states for wine ≈ 210K cases in 2020.
 - 452 Out of State Shippers applications received (Breweries, Wineries, Retailers) since October 2018.
 - 1389 Out of State Shippers as of November 1.
 - 221 In State Shippers as of November 1.
- Current enforcement includes review of filed shipper reports, work with common carriers to remove unlicensed shippers from services and outreach to unlicensed shippers to obtain licenses
- Staff allocations – Dedication of a consistent auditor and sworn agent to efforts was difficult due to turnover. With reduced on-premise activity due to COVID-19 we were able to dedicate resources
- Current allocations
 - 4 Full time auditors analyzing Common Carrier reports.
 - 3 Compliance Agents on a part time basis assigned to working on investigations and contacting unlicensed businesses.
 - 1 Part time License Technician dedicated to processing shipper applications.
 - 2 Compliance Agents on a part time basis assisting with processing applications.

Future Efforts on DTC

- Continue to engage the Common Carriers regarding their responsibility as a permit holder.
- Create an internal DTC Unit dedicated to Direct Shipping issues.
 - Received additional funding beginning in FY22
- Continue to engage unlicensed shippers and utilize the Common Carriers to prevent future shipments.
- Work on process to identify potential issues with Fulfillment Warehouses.

Public Safety Investigations

- **§ 4.1-225.1 Summary Suspension of ABC License:**

- The Board may summarily suspend any license or permit if it has reasonable cause to believe that an act of violence causing death or serious bodily injury has occurred on or adjacent the licensed premises, and the Board finds that there exists a continuing threat to public safety (Enacted in July 2016)
- Agents of the Bureau of Law Enforcement (BLE) have 48-hours to conduct an initial investigation to determine if the incident rises to summary suspension of the ABC License
- If initial investigation finds incident rises to Summary Suspension, the ABC License will be suspended for a minimum of 48-hours. Following initial suspension, BLE conducts a ten day formal investigation.
- The BLE investigates acts of violence at **all** establishments that have an ABC License
- Since 2016, the BLE has conducted 235 public safety investigations at ABC licensed establishments, that have led to 68 suspensions of ABC Licenses under this provision



Retail Operations

Growth of Omni-channel Fulfillment

Building / Warehouse & Systems

Freight Way Warehouse – Go Live

- Inbound Receiving
 - 04/12/21– Receiving calendar opened in new scheduling platform, first loads scheduled.
 - 04/19/21 – Warehouse open for inbound shipments of spirits. Inventory load in plan scheduled through the end of June.
 - Load in plan suspended May 21st, to address items related to building code.
 - Inventory load in plan resumed on 06/25/21.
- Revised outbound Go-Live
 - Original Go-Live date 07/15/21
 - Revised Go-Live date 08/23/21, planned cutover to the new facility two-weeks.
 - Ramp up schedule 1,200 cases day one, 2,000 cases day two, 3,200 cases day three, 6,500 cases day four with a goal to reach 25,000 cases by September 3rd.
 - Cutover to the new warehouse was delayed till October 6th, due to technical issues commissioning the case dispenser.
 - Case Dispenser is automated picking of the top 50 items accounting for 25% to 30% of daily case volume.
 - Dispenser operation stability was intermittent until 10/21/21.
 - Delay required prolonged operation out of two warehouses; adding inefficiencies and greater need for inventory.

Building / Warehouse & Systems

Freight Way

- Ship 35,000 cases in eight-hour shift
- 315,000 sq ft, expandable to 399,000
- High density storage, 36' clear span
- Inbound receiving doors 10, expandable to 15
- Outbound shipping doors 10, expandable to 15
- Automated dispenser, expandable double capacity
 - Ship top 50 items, two-person operation
- Manual case pick area, expandable by 20%
- Bottle pick area, expandable by 50%
 - Designed to accommodate future DTC shipping, pending future software implementation

Hermitage Road

- Ship 28,000 cases in an eight-hour shift
- 293,000 sq ft, land locked
- Bulk floor pallet storage, 24' clear span
- Inbound receiving doors 7, not expandable
- Outbound shipping 8 doors, not expandable
- High volume pick area, not expandable
 - Ship to 30 items, six-person operation
- Manual case pick area, not expandable
- Bottle pick area, not expandable
 - Would not accommodate DTC shipping



7450 &
7452
Freight Way

WABC



Store Growth

Current Store Count - 395

Fiscal Year 21

- Six Stores Opened (with six more locations in process)
 - Haymarket
 - Virginia Beach
 - Chesterfield
 - Prince William
 - Pentagon City
 - Warrenton
- Ten Stores Relocated (with 24 more locations in process)
 - Colonial Beach, Lynchburg, Deltaville, Midlothian, Virginia Beach, Vienna, Woodstock, Suffolk, Chesterfield, and Bon Air
- Four Stores Updated and Four Stores Expanded (with three more locations in process for expansion)

To secure business continuity during a national health crisis, Virginia Alcoholic Beverage Control accelerated their omnichannel priorities. In addition to addressing the immediacy of the pandemic, the effort aligned with long-term strategies to provide omnichannel fulfillment to the Commonwealth of Virginia.



- Spring 2020, Virginia ABC began development of scheduled curbside pickup at retail locations
- Provide customer with the ability to get contactless pickup
- Adoption has been extensive, approximately 70% of online orders take advantage of curbside scheduling

Launch Date: 04/04/2020
of stores: 381
Total Orders: 154,607
Total Sales: \$13,461,548
As of 12/2021



- Developed option of next-day shipping fulfillment via UPS
- There is a flat fee for next-day delivery
- Safeguards put in place with UPS to assure that IDs were properly checked to prevent underage distribution.
- Customers have ability track orders, choose window for delivery, and must be present to receive them.

Launch Date: 05/28/2020
of stores: 22
Total Orders: 5,345
Total Sales: \$540,271
As of 12/2021



- Development of same-day delivery via DoorDash began mid-2020
- Prioritized as a cornerstone of eCommerce capabilities
- Piloted in several stages, fulfills orders to customers within a 5-mile radius of the store
- Safeguards put in place to ensure proper ID checks

Launch Date: 07/21/2021
of stores: 285
Total Orders: 3,439
Total Sales: \$297,732
As of 1/2022

ON DEMAND FEEDBACK

Purpose: Gather feedback on customer experience related to on demand delivery service

Audience: On Demand Customers

Survey period: July 2021 – January 2022

Customer Responses

Honestly, I think you guys nailed it. DD did have a 10 dollar delivery fee which I would pay if I was in a time crunch like I was yesterday. The process was very smooth and I received alerts and that was great! There is a GREAT process for delivery! It took a minute but well worth it for safety. I'm in my 50's and that guy was not going to skip a step at all! super happy

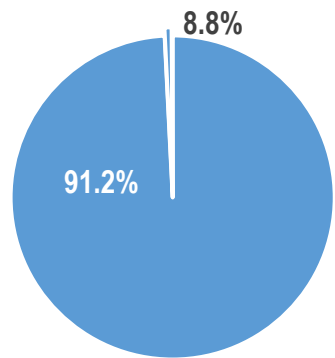
I ordered online at home delivery. The service was excellent and the order arrived in more than a timely manner. Thanks!

More Locations!

Entire catalog available for delivery, regardless of which store has stock.

I would like to be able to order products that aren't currently available at my local store, and have them delivered once they are transferred.

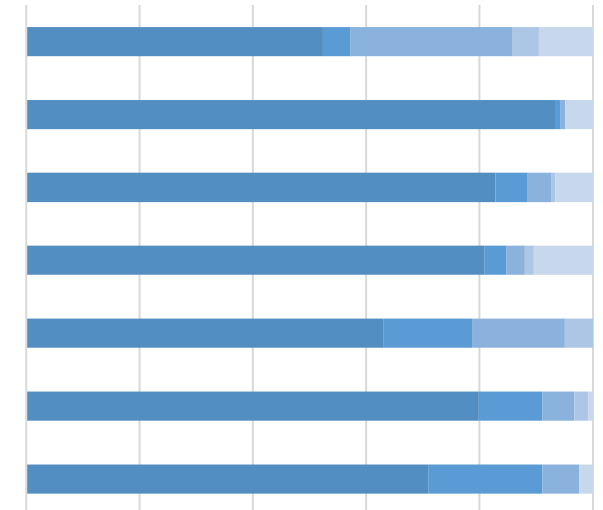
ID Compliance



■ Yes % ■ No %

Customer Satisfaction

- Customer Support was able to help me with any issues.
- I received all of the products I ordered in good condition.
- The driver was professional and delivery was smooth.
- My delivery arrived as scheduled.
- I was able to order the products I wanted.
- I was able to select my preferred day/time for delivery.
- The ordering process was easy.



■ 5 ■ 4 ■ 3 ■ 2 ■ 1

Rating Scale 1-5, 5=Best

Profit Forecast

Appropriation Act Profit Requirement

	<u>FY 2019</u>	<u>FY 2020</u>	<u>FY 2021</u>	<u>FY 2022</u>	<u>FY 2023</u>	<u>FY 2024</u>
Profit Transfer Required by Code	115,600,000	121,600,000	159,500,000	146,700,000	120,900,000	123,800,000
Department of Behavioral Health & Developmental Services	65,375,769	65,375,769	65,375,769	65,375,769	65,375,769	65,375,769
Auditor of Public Accounts	75,521	75,521	75,521	75,521	75,521	75,521
Department of Accounts	64,607	64,607	64,607	64,607	64,607	64,607
Department of the Treasury	47,628	47,628	47,628	47,628	47,628	47,628
Central Service Agency Support	169	169				
Operating Efficiencies	3,364,585	3,864,585	3,864,585	3,864,585	3,864,585	3,864,585
Deferred VRS	1,001,765	-	-	-	-	-
Total Profit Transfer Required	185,530,044	191,028,279	228,928,110	216,128,110	190,328,110	193,228,110
Actual Profit Transfer	196,657,876	212,090,014	237,299,273			
Actual Transfer above Required	11,127,832	21,061,735	8,371,163			

Financial Forecast – Revenue (Sales)

Sales Forecast – 1.23% increase in FY22 and FY23; 3% in FY24

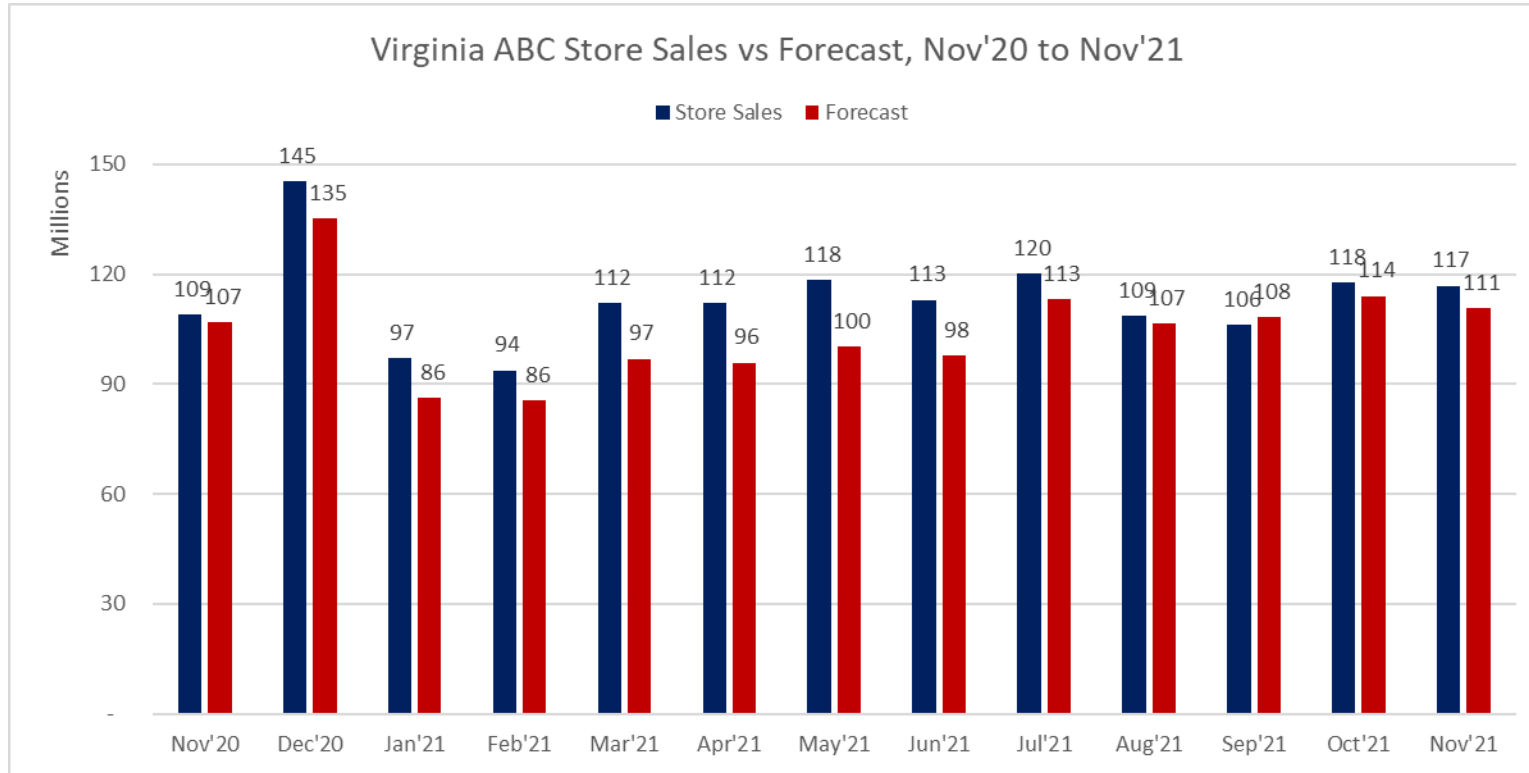
- Retail Volume - up compared to FY21, but barely
 - Projecting growth just over 1% due to huge jump in FY21 (13.4%)
 - Spirits growing as a category compared to beer and wine
 - Continued supply challenges and economic uncertainty, including inflation, could limit premiumization by consumers, a major component of growth
- Licensee Volume - up compared to FY21, but uncertain
 - Traditionally, licensees account for 18% of ABC sales
 - Licensee sales have rebounded to pre-pandemic levels, but unclear what lies ahead due to changed customer behavior, continuing pandemic and worker shortages

Virginia ABC revenue growth has both headwinds and tailwinds

- Store Growth – FY22 to-date and planned
 - Currently have 395 stores opened, three more than at this point last year
 - One store has opened in FY22 generating \$1M of store sales, six stores opened in FY21 generating \$8.6M of store sales in FY22
- Licensee Sales
 - Sales to licensees rebound to 16% in FY22, consistent with pre-COVID levels, but with higher revenues as the Authority's revenue has grown
- Out of Stocks
 - Product out of stocks at all time high, driven by demand and supply disruptions, reaching 6-12% vs normal 1-2% in distribution center
 - Suppliers face continuing challenges with staffing, receiving raw ingredients or packaging, transporting product, and importing product
 - Both in-bound and out-bound shipping challenges exacerbate store level shortages
 - These out of stocks have challenged customers who sometimes cannot locate an alternate spirit of choice
- COVID-19
 - Massive revenue growth during COVID, unlikely to be sustained and already slowing down
 - Negative operational impacts, with store closures from both COVID exposure and staffing issues
 - Diminished staffing in the distribution center can drop shipping levels by 10,000 or more cases in a day
- eCommerce
 - ABC grew eCommerce capabilities, with utilization much higher than pre-pandemic levels; further investment needed to realize potential
- Inflation
 - Heightened inflation putting pressure on consumer purchasing power
 - Some suppliers already taking price increases, others likely to follow suit

Store Sales vs Forecast: Store sales remain favorable

Store sales were \$6.1M favorable in November, or 5.5%, and store sales are favorable by \$19M for FY21 to date. Late FY21 growth resulted in most FY22 budgeted growth to be front loaded to first half of the year, so we have updated the budget to be more accurate.



Source: SmartView

Notes:

- November continued to deliver sales levels consistent with post pandemic, with \$116.8 million of sales, beating forecast by \$6.1 million, or 5.5%
- External industry data suggests that some of the higher revenue seen could be permanent, but concerns remain on a variety of risks, and sales volatility remains
- Risks include: product out of stocks, pace of inflation, potential impact of COVID variants



Store Sales are \$19M above FY22 budget thru Dec 31, 2021

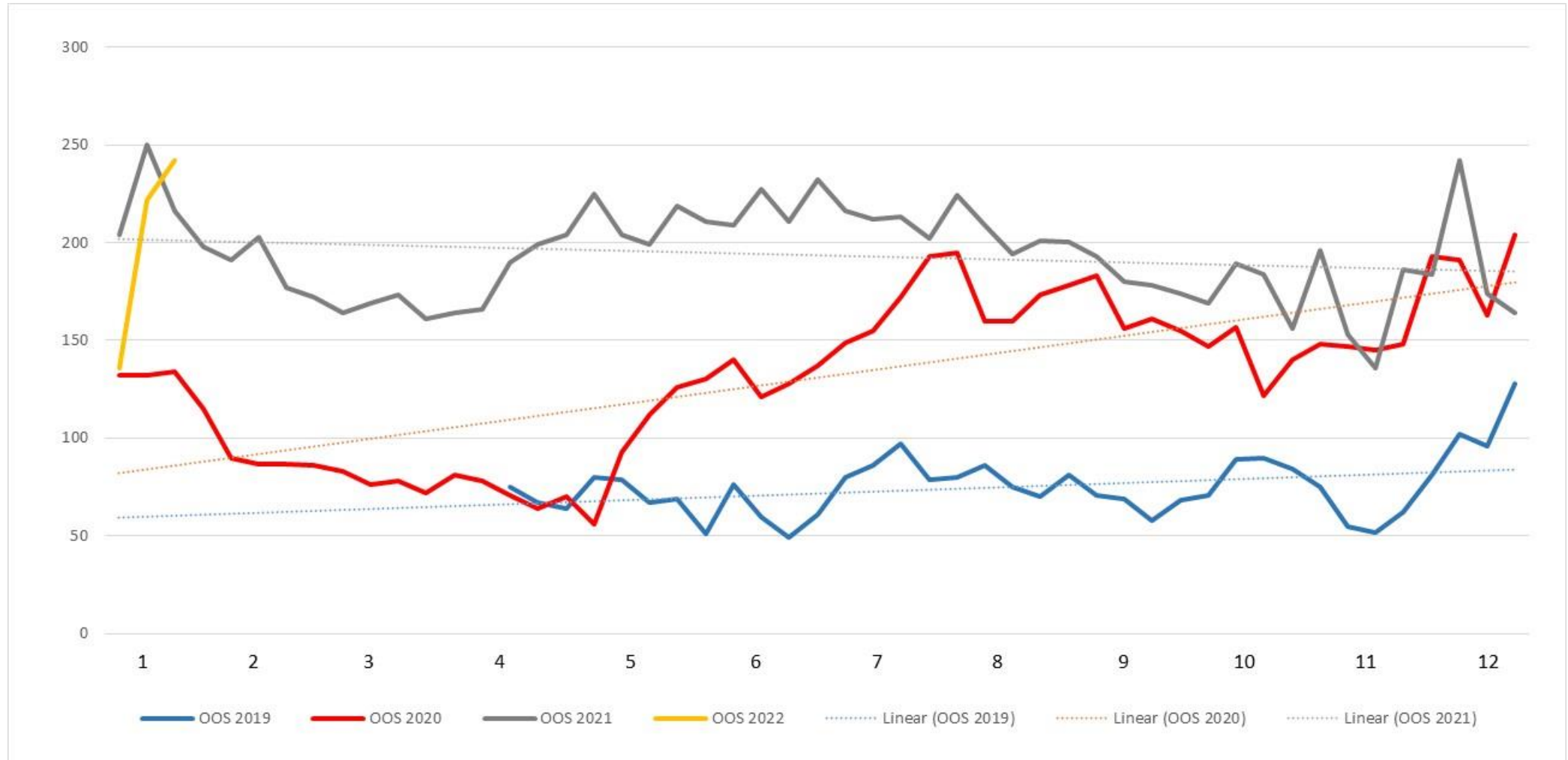
Sales remain volatile, with inconsistent monthly growth versus prior year. However, it's the extraordinary growth in the final months on FY'21 that represents the biggest risk for FY'22, as growth in those months will be challenging to exceed.

<i>In \$M</i>	Jul'21	Aug'21	Sep'21	Oct'21	Nov'21	Dec'21	Jan'22 (thru 1/16)	YTD
Actual	120.3	108.7	106.1	117.9	116.8	152.8	47.6	770.2
Budget	113.3	106.7	108.2	114.1	110.8	150.9	47.2	751.1
Variance B/(W)	7.0	2.1	(2.0)	3.8	6.0	1.9	0.3	19.1
<i>FY'21 Actual</i>	<i>111.9</i>	<i>105.3</i>	<i>102.2</i>	<i>114.1</i>	<i>108.9</i>	<i>139.2</i>	<i>47.9</i>	<i>729.6</i>
<i>Growth vs FY'21</i>	<i>7.5%</i>	<i>3.2%</i>	<i>3.9%</i>	<i>3.3%</i>	<i>7.2%</i>	<i>9.8%</i>	<i>-0.8%</i>	<i>5.6%</i>

Notes:

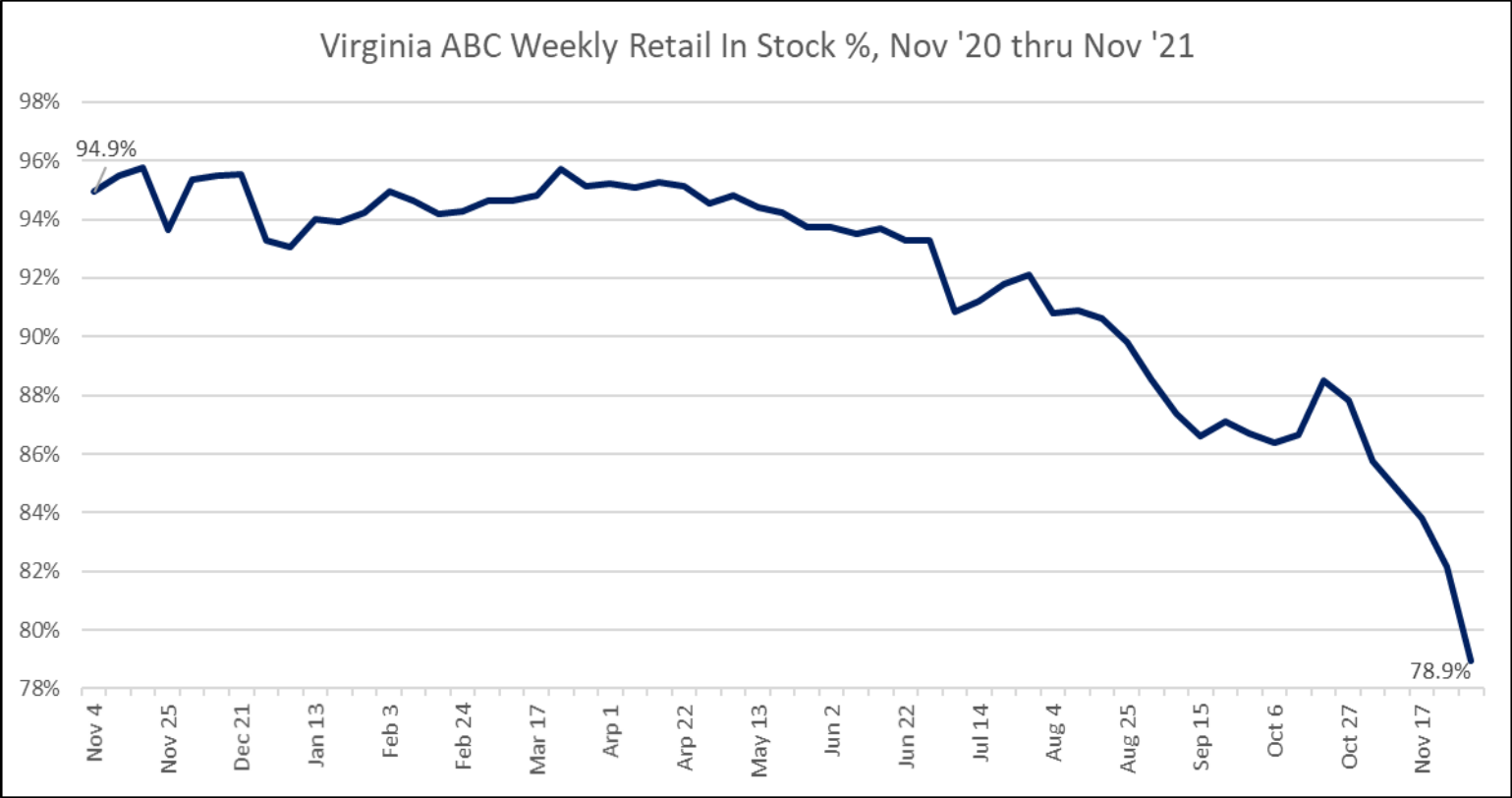
- Revenues remain volatile, with little correlation to historical trends
- External industry data suggests that some revenue growth from COVID will be permanent, but the lower favorability over the most recent months makes the level of retained incremental revenue uncertain
- January and February are the historical slow months for store sales
- March thru June sales in FY21 were 9.1% higher than FY20, which were already inflated from the pandemic, and may make it difficult to duplicate the sales levels needed to meet/exceed budget in those months in FY22
- At this point last FY, store sales were \$65M higher than budget, demonstrating the difference between FY21 and FY22
- Additionally, product out of stocks and inflation impacts on discretionary spending are materials risks to store sales

Out of Stocks 2019 - 2022



Retail In Stock %: Negative impacts from COVID continue to drive OOS

Retail stocks remain impacted from both increased demand and supply chain difficulties, but did improve slightly in October as holiday deliveries began flowing into the distribution center.



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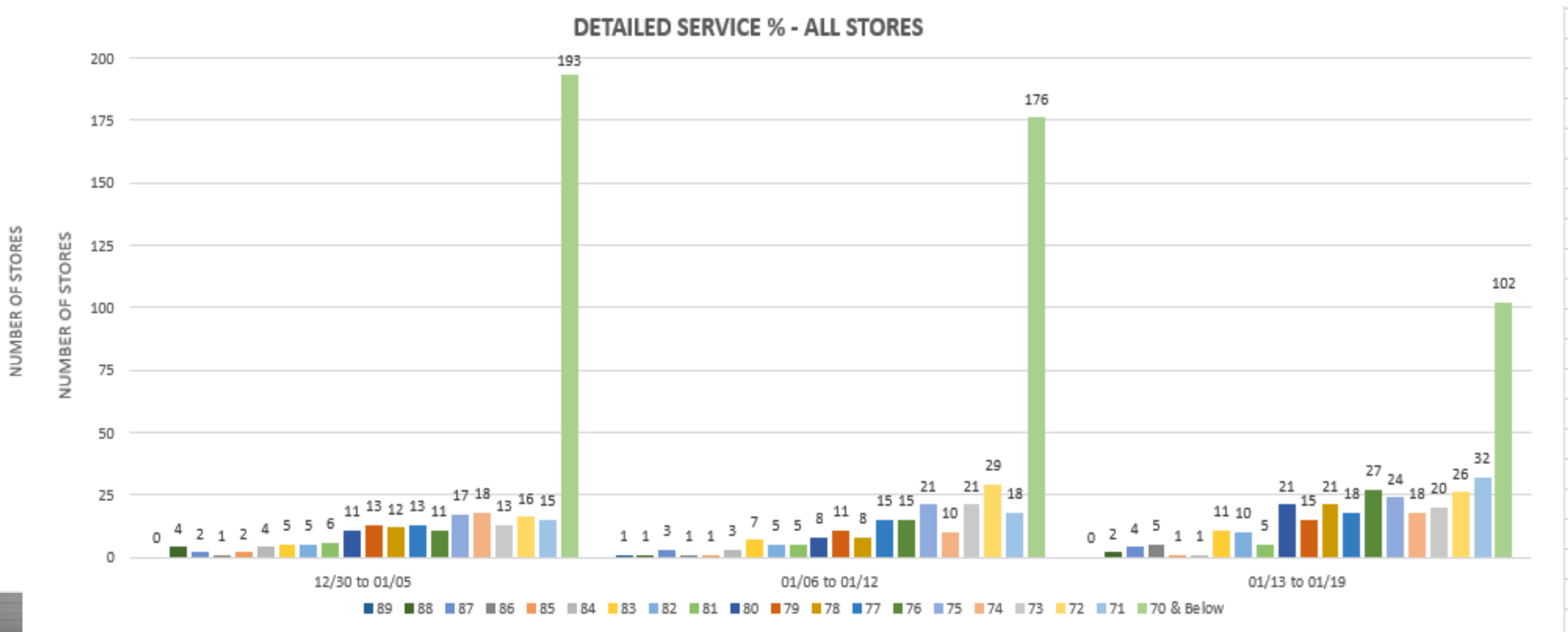
- Improvements seen earlier in the year have been completely reversed out
- Suppliers are indicating they are allocating product to balance demand across their portfolio of customers
- The elevated sales increases will continue to challenge supply for the foreseeable future

Source: Logistics



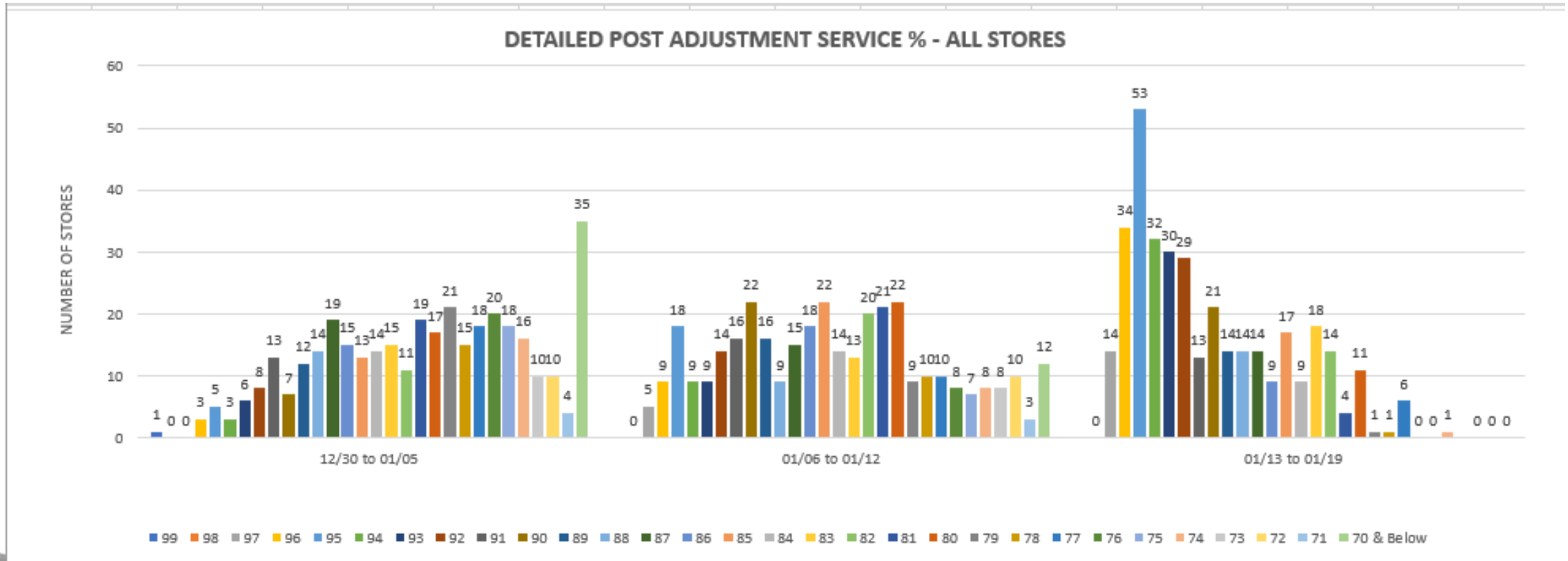
In-Stock Levels for All Stores

- Considerable out of stocks at retail and wholesale, but seeing improvement



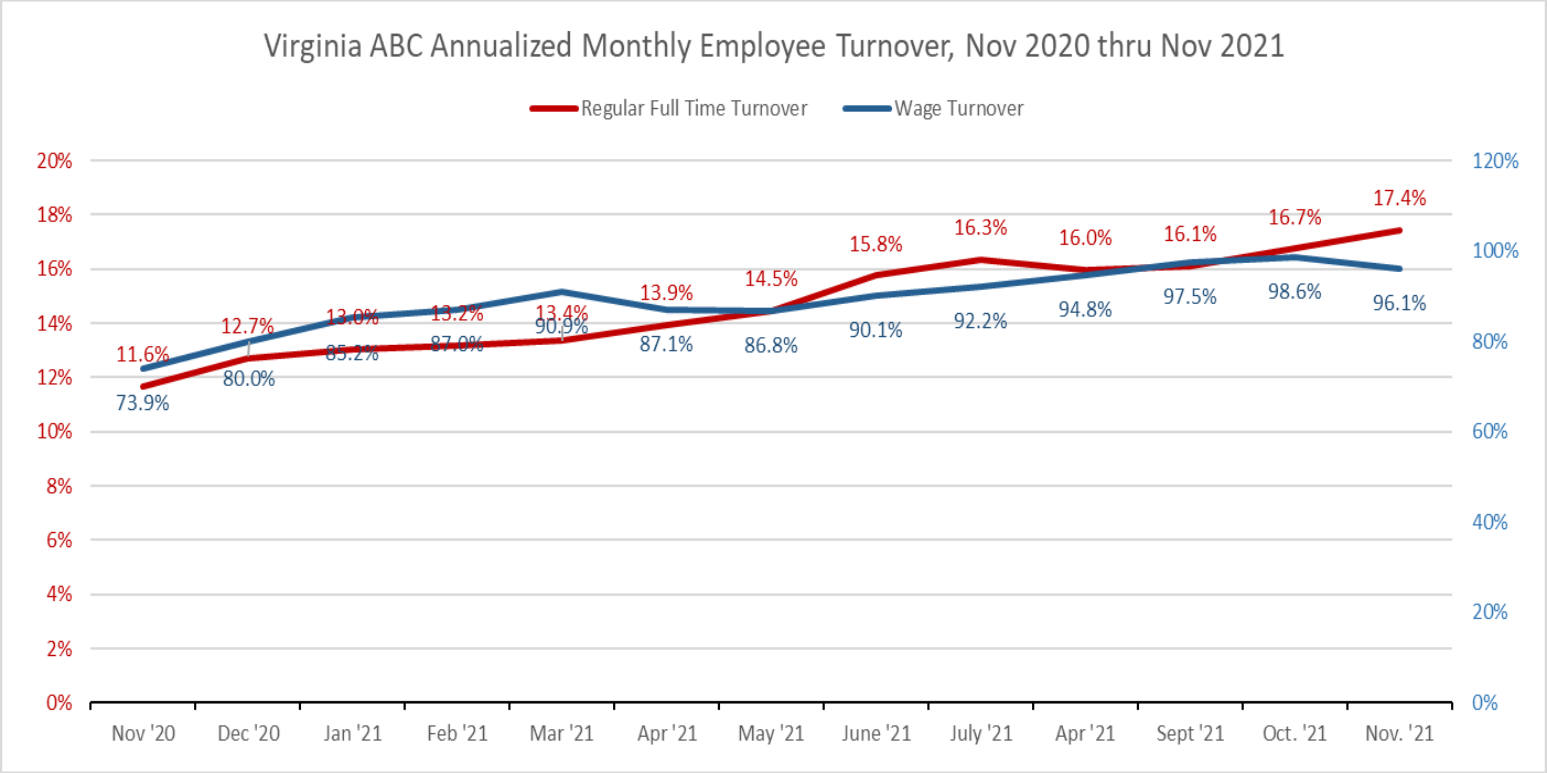
In-Stock Levels for All Stores with Wholesale Out of Stocks Removed

- Taller bars to the left indicate trend toward higher inventories in stores



Employee Turnover: Both wage and staff turnover rising

Turnover for full time employees has flattened over the past few months, while wage (primarily store and distribution center staff) turnover has increased after flattening out in the spring.



Notes:

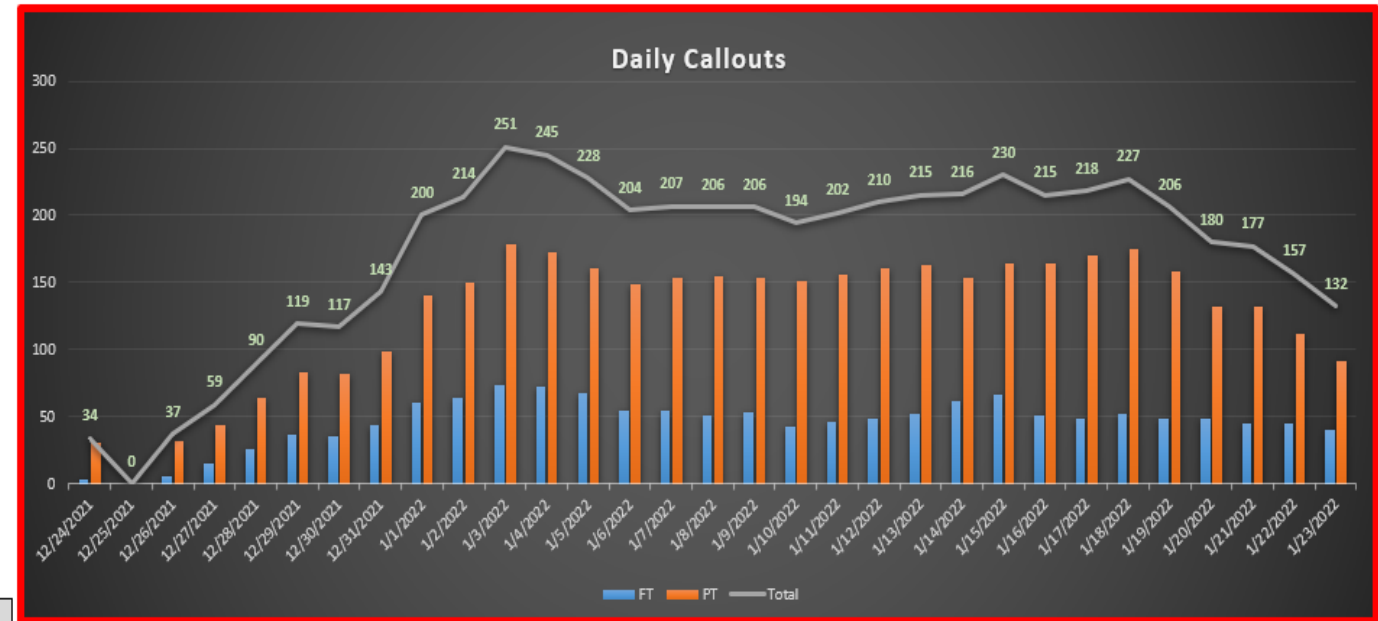
- Employees finding alternative employment remains the number one factor contributing to increased turnover for wage employees.
- Pay increases by the Authority is the likely reason for flat turnover amongst full-time employees.

Source: HR System Query



Increasing Callouts Impacting Retail Operations

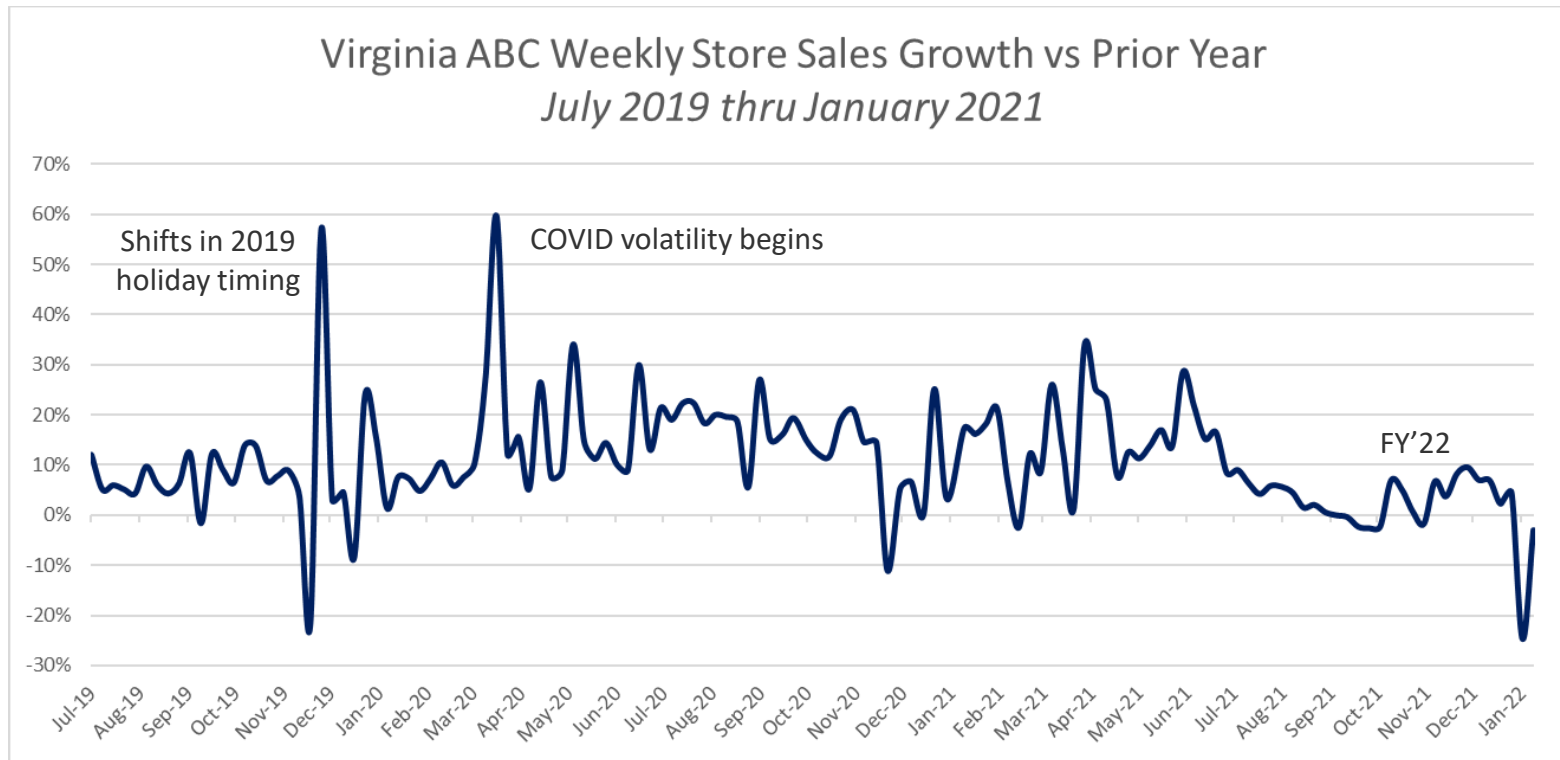
- Unanticipated callouts lead to early store closures or delayed openings
- Place greater strain on employees who remain
- If callout COVID related, may result in quarantine where employee not available for future scheduling
- A COVID positive employee can also result in close contacts for other employees, and additional quarantines
- Reducing store hours allows us to better allocate personnel to maintain operations and gives customers greater predictability



Today	Positions	12/23/2021	12/24/2021	12/25/2021	12/26/2021	12/27/2021	12/28/2021	12/29/2021	12/30/2021	12/31/2021	1/1/2022	1/2/2022	1/3/2022	1/4/2022	1/5/2022	1/6/2022	1/7/2022	1/8/2022	1/9/2022	1/10/2022	1/11/2022	1/12/2022	1/13/2022	1/14/2022	1/15/2022	1/16/2022	1/17/2022	1/18/2022	1/19/2022	1/20/2022	1/21/2022	1/22/2022	1/23/2022
1/23/2022	FT	1	3	0	5	15	26	36	35	44	60	64	73	72	67	55	54	51	53	43	46	49	52	62	66	51	48	52	48	48	45	45	40
	PT	33	31	0	32	44	64	83	82	99	140	150	178	173	161	149	153	155	153	151	156	161	163	154	164	164	170	175	158	132	132	112	92
	Total	34	34	0	37	59	90	119	117	143	200	214	251	245	228	204	207	206	206	194	202	210	215	216	230	215	218	227	206	180	177	157	132

Sales volatility has lessened, but suggests lower growth in FY22

Sales growth steadily trended lower during the first few months of FY22, and growth is lower than seen in FY19 prior to the pandemic's start in the spring.



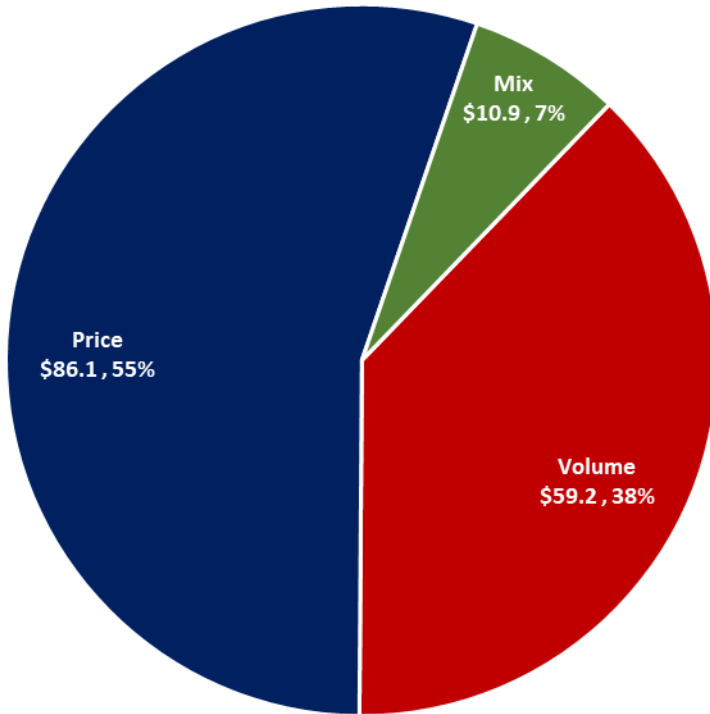
Notes:

- At the end of February 2019, before the pandemic changed consumer shopping habits, Virginia ABC's FY19 sales were ~7% higher than FY18
- Although sales were volatile, once the pandemic impacts started, they maintained higher lift from March 2020 thru June 2021, generally averaging 9%+
- For FY22, that trend has changed, and the first four months of the year showed a steady decline from 10% to declines, before rebounding during the holidays, historically the strongest sales timeframe for Virginia ABC
- Immediately after the December holiday, sales dropped, likely driven by the combination of high levels of product out of stocks, lower demand driven by inflation reducing discretionary spending

Virginia ABC store sales increased by \$156M in FY21, or 13.4%

The biggest driver for the increased sales was higher average per bottle prices, primarily caused by premiumization. This premiumization growth isn't likely to be duplicated, especially with prevalent out of stock issues and inflationary pressure on discretionary spending.

Virginia ABC Store Sales Analysis: FY'21 vs FY'20
Revenue Change Drivers



- Volume/Price/Mix analysis identified that \$86M of the \$156 M increase, or 55%, was driven by increased price per bottle
- Further analysis of this \$86M increase revealed that \$12M, or 14%, of the increased revenues was driven by changes in pricing; the bulk of the increase was from premiumization, with consumers choosing more expensive products at a higher rate
- Much of this premiumization was a change in consumer behavior that started at the beginning of the pandemic at the end of FY'20, and represented the full annualized impact of that change in shopping behavior
- Normal premiumization trends have resulted in ~1% of Virginia ABC store sales growth in the years leading up to the pandemic, but the level of out of stocks driven by supply chain issues, combined with inflationary pressure on discretionary spending, will make premiumization growth unlikely in the near term.

Additions to Forecast for FY 22

- **Adjustments to Compensation**

- 5% State pay increase for all employees + 3% pay increase and years of service bonus for all sworn enforcement officers
 - ABC received partial profit transfer relief for the initially estimated 3% salary increase but not the full 5% increase.
- Board approved 3% pay increase for all ABC employees + extra 2% for sworn enforcement officers.
- In June 2021, ABC built in retail base pay the “service commitment pay” that had started during the pandemic
- In December 2021, ABC implemented adjustments to Central Office and Enforcement pay in December pursuant to recently completed independent classification and compensation study
 - Adjustments targeted market midpoint for positions
 - Classification system built to reflect personnel needs specific to Virginia ABC
 - Study found 55% of ABC Central Office and Enforcement positions needed adjustment, with 24% of salaries below the recommended minimum
 - Law Enforcement positions had only 18% of roles priced near the midpoint. Over 40% of their positions fell below the minimum expected salary for the role.
- Further Adjustments to Retail and Distribution Center planned for FY23.

- **ABC Property**

- Depreciation/amortization of new facility begins FY22
- Sale of the old ABC Building projected to yield a one-time gain of 14.7M if completed in FY22

- **Dual operation cost**

- Operating both warehouses during first half of fiscal year
- ABC will incur expenses of winding down Hermitage Road facility

- **Supply chain operations**

- Rising freight cost due to driver shortage
- Increased distribution center staff due to volatility in the workforce
- Equipment purchases to support increasing shipping volumes

- **COVID Anticipated cost of \$4.2M**

- Testing Kits – Projected cost - \$1.5M
- Cleaning and related costs – Projected cost \$2.7M

Additional Expenses Forecast for FY 23 and FY 24

- **FY23 Additional Expenses**

- Full-year implementation of compensation adjustments
- Store Growth Salary and Wage Impact of \$4.1M for new store openings, adding positions to stores due to growing operational complexity and increased store operations support staff
- Mid-year implementation of adjustments to retail and distribution center compensation to maintain competitiveness in market

- **FY 24 Additional Expenses**

- Store Growth Salary and Wage Impact of \$2.8M for new store openings, adding positions to stores due to growing operational complexity and increased store operations support staff
- Full-year impact of adjustments to retail and distribution center compensation
- Increased credit card fees of \$1.3m in line with 3% sales increase
- Increased project amortization \$2.5M (principally HR system and Website redesign)

GACRE Forecast FY 22 - 27

As of 10/29/2021 (1)

(in millions)

	Forecast					
	FY2022	FY2023	FY2024	FY2025	FY2026	FY2027
Revenue Sources:						
	<i>Growth Rate</i>	1.23%	1.23%	3.00%	4.00%	4.50%
Alcoholic Beverages (Store Sales)		1,350.0	1,366.6	1,407.6	1,463.9	1,529.8
Less: State Taxes on Spirits & Wine		224.8	227.5	234.4	243.7	254.7
Net Store Sales		1,125.2	1,139.1	1,173.2	1,220.2	1,275.1
Other Revenue		35.9	22.9	23.4	23.8	24.3
Total ABC Revenue		1,161.1	1,162.0	1,196.6	1,244.0	1,299.4
Cost of Goods Sold:		650.7	658.7	678.5	705.6	737.4
Operating Costs:		295.4	305.9	314.7	325.0	336.1
Infrastructure Projects (2):			7.1	10.2	10.6	10.6
ABC Net Profit		215.0	190.3	193.2	202.8	215.3
Profit Carryover from Prior Fiscal Year		1.1				
ABC Profit Requirement & Mandatory Transfers (3)		216.1				
Over/(Under) Required Transfer		0.0				

Notes:

1. Forecast developed on accrual basis. The profit transfer occurs on a cash basis. Variances often occur at year end when ABC has to transfer estimated profits prior to June 30th.

2. Infrastructure projects are ongoing and the depreciation/amortization impact with an increased impact beginning in FY23. These projects include the Body worn camera and ecommerce project. All live projects as well as projects that will be going live in FY22 were included in the FY22 base budget.

3. HB/SB29 Caboose as adjusted for duplicated \$14.7M Gain on sale of Hermitage Road property



FY 23-24 Budget Items



eCommerce Implementation Project



Body Worn Cameras Project



Store Network Growth



Store Clerk Conversion

eCommerce

eCommerce Investment: Pandemic identified need for stronger capabilities

Increased ordering activity during COVID highlighted problems in the current state of eCommerce capabilities, especially in our ability to meet customer expectations for online purchasing experience.



Current State:

- Poor customer interface
- Inconsistent experience with focus on selected store inventory
- Unreliable website performance
- Limited communications ability
- No cross-marketing ability
- Fulfilment option not available until end of order process



Investment Opportunity:

- Three phase project over two and a half years will deliver new capabilities that increase customer engagement with a product centric experience.
- A new eCommerce platform will provide a user-friendly interface, and effectively increase communications to customers during and after an order is placed.



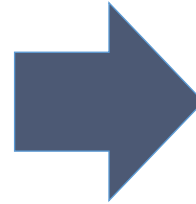
Future State:

- An information-based product-driven experience
- Customers can take action wherever they are in the process and the next step is crystal clear
- Reliably able to support the demand and traffic on the website
- Seamless omnichannel shopping and data integration

eCommerce Investment: Sales estimates suggest strong potential growth

- U.S. online alcohol sales reached \$6.1 billion in 2021
- Online sales represent 4% of all off-premise alcohol sales in the U.S., up from 1.9% in 2019
- Online alcohol sales are projected to grow an additional 3.4% in 2022
- ABC estimates eCommerce investment could deliver >\$40M in net margin in the first five years, after one time and ongoing expenses are covered.

Virginia ABC: E-Commerce Investment		
Metrics Changes		
	Target Growth	Likely Range
Add to Cart Increases	7%	3-15%
Funnel to Checkout	14%	5-30%
Avg Bottle Price	\$0.46	\$0.25-\$1.00
Increased Orders	10%/yr	5-20%
Premiumization	0.34%/yr	0.15-1%
New Customers	10%/yr	5-20%



Virginia ABC: E-Commerce Investment	
<i>In \$M</i>	First Five Years
New Online Sales	162.3
Gross Margin	56.8
One Time Project Expense	(7.0)
Ongoing Expense Impacts	(7.2)
Net Margin	42.6

- New Online Sales amounts have been forecasted based on the estimated impact on specific sales metrics across the online sales funnel: number of people going to the eCommerce site, how frequently they visit the eCommerce site, how often they put products in the shopping cart, how often they move to to checkout, how many bottles they purchase, and the average price of the bottle they purchase
- Gross margin represents revenues after cost of goods sold and excise taxes (does not take impact of excise taxes into account for the Commonwealth)

eCommerce Investment: Will require both one time and ongoing expense

In working with external consultants, one time project costs of \$7.0M have been estimated, as well as ongoing costs of \$1.7M per year, which includes 8 incremental MEL. However, these estimates are still being refined, and subject to procurement.

Virginia ABC eCommerce Investment Opportunity

One-Time Implementation Expense	(\$M)
Software/Licenses	1.4
Labor	<u>5.5</u>
Total One-Time Expense	7.0
Annual Ongoing Expense	(\$M)
Software/Licenses	0.6
Labor	<u>1.1</u>
Total Ongoing Expense	1.7

- One time project expenses are just the costs to implement the investment and include external labor (outside implementation support), licenses for the eCommerce platform, internal labor and 15% contingency
- Ongoing expense impacts represent additional costs required to administer the eCommerce system, content, and customer support for the new site
- Ongoing expenses include software and license costs, as well as eight additional MEL for front-end system support, back-end development, information security, and three customer support agents
- There are other potential expenses not yet accounted for, such as marketing of the new site, new features and fulfillment options
- All expenses estimated with an external consultant, and will be refined during procurement and hiring processes

Body Worn Cameras

- Implementing body worn cameras for ABC agents
 - Use of BWC is becoming a recognized best practice for law enforcement agencies
 - Can protect the public as well as the involved officer
 - Will provide BWCs to all field agents
 - Expense for hardware, software & storage
 - FY23 - \$391K
 - FY24 – \$372K
 - 1 MEL to serve as digital evidence custodian and data analyst
 - \$130k with benefits

Store Growth

- Personnel needed for the growth of new ABC Retail Stores
 - Each new store receives at least two FTE and sufficient part-time workers
 - Stores growing in volume receive additional FTE to support sales
- Request includes other support positions for store growth that have not been considered in the past
 - Property Management
 - Logistics
 - Human Resources and Payroll
 - Procurement and IT
- Net increase of 36 stores and 1113 retail store employees since 2016
- No change in support staff to accommodate the growth

Store Clerk Conversion

- Converting 25 part-time positions to 25 full-time positions in each year of the biennium – total of 50
- FTE positions provide greater stability in the short-term and with long-term retention
- Expenditure is partially offset by reduced part-time positions as well as diminished costs related to employee turnover
- FY23 expenditure of \$867,000
- FY24 expenditure of \$1.7M



Questions

