US Pod Coffee Market Poised For Further Expansion

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As US coffee pods transition from niche product to mainstay, category leaders in Western Europe provide insights for future growth.

The US fresh ground coffee pod industry is dominated by one name: Green Mountain. But, despite reporting impressive results in early May, Green Mountain Coffee Roasters (GMCR) stock tumbled as this figure was well below the 50% growth the company had sought.

Many analysts commented on GMCR's inability to forecast its market, while noting the uncertainty the company faces in light of its coming patent expirations. But whether or not GMCR will lose share once their monopoly on the K Cup model expires, coffee pods as a market are here to stay. By examining how the US pod market has merely scratched the surface with its exponential growth, and how pods fared similarly in Western Europe, specifically France, it is clear that pods are changing the way more and more Americans consume their coffee.

US single serve coffee market on the rise
Fresh ground coffee pods have exploded in the US over the past five years, growing retail volume by 523% from 2006 to 2011. Click to tweet! Â Once niche products, pod machines have become increasingly popular in workplaces and households, with pods now available in mainstream grocery stores and hypermarkets, led by products from foodservice brands like Dunkin' Donuts .

While pod penetration is still relatively low compared with other types of coffee in the US, single-serve coffee pod machines now account for 20% of total coffee machine volume sales, up from 4% in 2006. Click to tweet! Total coffee machine sales are projected to increase by 20% from 2011 to 2016, largely driven by pod machine expansion. Consequently, fresh ground coffee pods are expected to lead growth within coffee from 2011 to 2016 with off-trade volume growth of 74%.

In many ways, the rapid expansion in pods now underway in the US mirrors that seen in Western Europe years before, where pods now hold significant share. While fresh ground coffee pods represented a mere 2% of all US off trade fresh coffee retail volume in 2011, they held a 23% share in France, which saw a large spike in coffee pod volume in 2005, with 26% growth, followed by 35% growth in 2006, thanks to pod and pod brewer manufacturers Kraft Foods (Tassimo) and Sara Lee (Senseo) spending almost US$10 million each on advertisements promoting their machines' ability to provide customers with a convenient product of professional quality. With consumers increasingly leading on-the-go lifestyles, pods quickly became a hit as the machines allowed them to brew single serve cups of coffee similar to beverages they purchased in local cafÃ©s.

Many believed that the global economic downturn would present difficulties for pods as they were both priced and positioned as a premium product. However, share actually grew as premium brewers such as NestlÃ© SA's Nespresso line targeted high income households.
Combined with the more affordable Senseo machines, which had already penetrated medium/low income homes, coffee pods underwent a segmentation that further engrained them into coffee culture. This premiumisation resulted in the more expensive coffee pods surpassing standard fresh ground and fresh coffee beans in retail sales, accounting for more than 50% of retail sales value. It became clear that consumers in France will pay more for the quality and convenience of pod coffee.

Brewers prepare for market growth and price segmentation
Like the French, Americans are regularly on the go, and, given the success of foodservice specialty coffee shops, consumers have developed an appreciation for high end fresh brewed coffee. But to assume that the US pod market will mirror France ignores significant differences between the two. On a per capita basis, Americans consumed 276.4 off trade cups of coffee in 2011 compared to 395.1 in France. Click to tweet! Coffee in France is often consumed in the smaller and stronger espressos or cappuccinos rather than the larger â€œcup of joeâ€• preferred by most Americans. The average French cup of coffee is 150 mL, brewed with 45 g of coffee per litre compared to 300 mL and 32 g per litre in the US, respectively.

The French also consume coffee drinks multiple times in the day, as part of social gatherings whether it be on-trade or at home, while the US market remains heavily skewed towards morning consumption. Because of these fundamental differences in consumption, it is unrealistic to think that the US market can reach the levels of France; however, as manufacturers continue to provide consumers with customisation and price segmentation, pods will continue to take share from other coffee types.

The Keurig has found success in the US while the higher priced Nespresso has struggled, owing to Keurig's speed and ease of use in producing a high quality cup of coffee more appealing for American consumption, rather than the â€œEuropeanâ€• coffees that Nespresso recreates.

Combine this with the licensing agreements between Keurig and many popular specialty coffee brands like Caribou, Starbucks, and Dunkin' Donuts, and US consumers can use the machines to recreate the on-trade experience and thereby give a perception of quality at lower price points. Furthermore, once GMCR's K cup patents expire in September 2012, more coffee roasters will make pods for Keurig machines, thereby driving prices further down and making the product more accessible to consumers.

As more consumers become exposed to the pod format, manufacturers are also becoming more cognizant of the importance of customisation. Companies such as Nespresso, Starbucks, and GMCR are banking on economic recovery as an indicator that the US will mimic France's pod brewer segmentation. NestlÃ© hoping increase in spending will increase the sales of the Nespresso amongst higher income consumers seeking espressos and cappuccinos.

GMCR launched its next generation pod brewer, the Vue in March 2012, touting its ability to customize drinks and produce cafÃ© beverages such as lattes. And Starbucks has announced a holiday release of its Verismo single cup brewer, which the company claims will be able to produce the perfect lattÃ© due to new technologies with milk pods.

With household penetration rising and players such as Starbucks entering the premium brewer market, exposure for single cup machines will only increase, thereby pushing the market further. These new pod varieties and brewers will go a long way toward providing the customisation and differentiation that succeeded in France.

So, while it may be overly optimistic to assume the US will follow Western Europe in terms of penetration, pod share, and consumption, it is realistic to envision a market where pod present a real threat for other coffee types.

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