Craft-beer-ship: Breaking the Barriers in Beer Industry

Boston Beer Company – Pioneering the Shoaling and Micro-brewery Strategy

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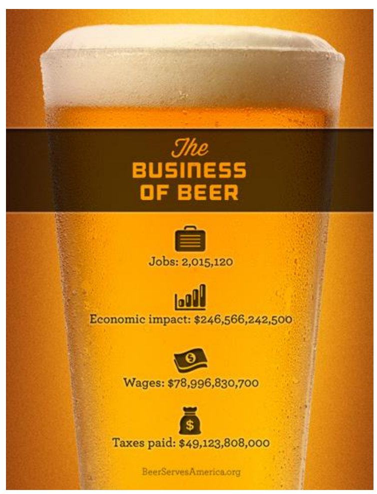


Often industry forces favor the established large players by creating strong barriers to the small firms and new entrants. Large established firms enjoy high bargaining power against suppliers and buyers and reduce the threat from substitutes or industry rivalry through mergers and acquisitions, increasing market share concentration and asset consolidation, capacity building, cost leadership, price signaling, regulatory advantages, and so on. With sheer size and scale based advantages - giving the appearance of more consumer surplus - large firms tend to arm-twist the actors in the value chain to gain more advantage, and thus shall reduce the choices available to customers and can stifle the industry growth and innovation. The beer industry is one case where integration/ consolidation is routinely pursued to grow as well as to ward off the problems of mature industry like intense rivalry, low-profits, and price wars. In many industries, such a consolidation scenario is neither good for customers nor society at large.

More than anti-trust regulations, new entrants and industry revolutionaries can do a great favor to customers and the whole industry if they can break the barriers and change the rules of the industry through innovation in products or production and organization methods. Boston Beers is one such case of breaking barriers and pioneering industry transformation through several strategic innovations. Boston Beers has built a business model based on 'value-chain cooperation and shoaling' rather than consolidation or domination. This model is proven to be more effective in generating profits and sustaining growth than the traditional route of mergers.

Boston Beer Company is one of the most successful craft brewers in the United States competing effectively against large mass-producing breweries. "Boston Beer" was founded by Jim Koch in 1985 with a family recipe and entered the market with a crafted beer brand "Samuel Adams Lager". This brand was initially brewed in small batches with an obsession for quality, freshness and flavor. Samuel Adams beers have won numerous international awards and are still brewed using the time-honored, traditional four-vessel brewing process and are market positioned in the "Better Beer Category". Samuel Adams is the only brewer practicing a cooperative program with its distributors to buy back its beer when it is past its peak freshness date.

Samuel Adams brand boasts itself as high-quality hand-crafted beer made with world's finest all-natural ingredients purchased from Bavarian hops farmers. Instead of locking all the capital in production assets, Boston beer has grown primarily through microbrewery production methods and contracting with third-party packers and franchisees to produce all its brands. Boston Beer has launched more than 500 varieties, and released 25 new beers in 2012 and brewed another 55 in-house.

With the strategy of operating in a decentralized and dispersed manner using a chain of contract brewers, Boston Beer was able to market its specialty crafted beers nationally without incurring shipping expenses. From 500 barrels per year during its inception years to brewing close to 4 million barrels per year now, Samuel Adams has grown to be the largest craft brewer with 1 per cent of the total US beer market (www.bostonbeer.com). Samuel Adams brand has become an inspiration and a catalyst to other small and microbrewers. The exemplary performance of microbrewers and specifically specialty craft brewer like Boston Beer Company serves as a testament to the effectiveness of the business strategy of disaggregation and dispersion of manufacturing, marketing and distribution activities. Boston Beer's strategy illustrates how firms can operate profitably in a smaller scale disaggregating their core activities achieving variety, quality, uniqueness and customization. And this shoaling strategy can be effectively replicated in a range of businesses and industries such as food processing, consumer durables and construction for achieving innovation and growth.

In addition to the cost and marketing-related advantages, there are several socio-economic benefits of disaggregating a firm's value chain. Through disaggregation of operations, a firm can decentralize decision making and provide more autonomy, and thus in turn can develop a sense of ownership among employees and managers. Disaggregation allows for more product or design variations in manufacturing. Decentralized operation enables simple and lean organization structure, reducing the power and salary distance between management and employees. Dispersed value chain allows unit and functional level managers to search for new opportunities resulting in diversification and growth. With dispersed operation of the value chain, there is more opportunity for sharing or franchising the firm ownership with managers and employees, and thus reducing the cost of capital and investment risk. Dispersed arrangement helps firms to develop multi-pronged competitive strategies, that is, enabling the firm to develop a unique or optimal strategy for each rival it encounters in the respective market or region. In addition to achieving cost reduction, quality and customer responsiveness, dispersed operations would help companies reduce the environmental cost and enhance the sustainability performance. Samuel Adams's overall success in terms of cost savings, quality, innovation, employee learning and productivity, and overall effectiveness in terms of financial and operational performance attest to the significance and consequence of scale reduction and dispersion of organization and production systems.

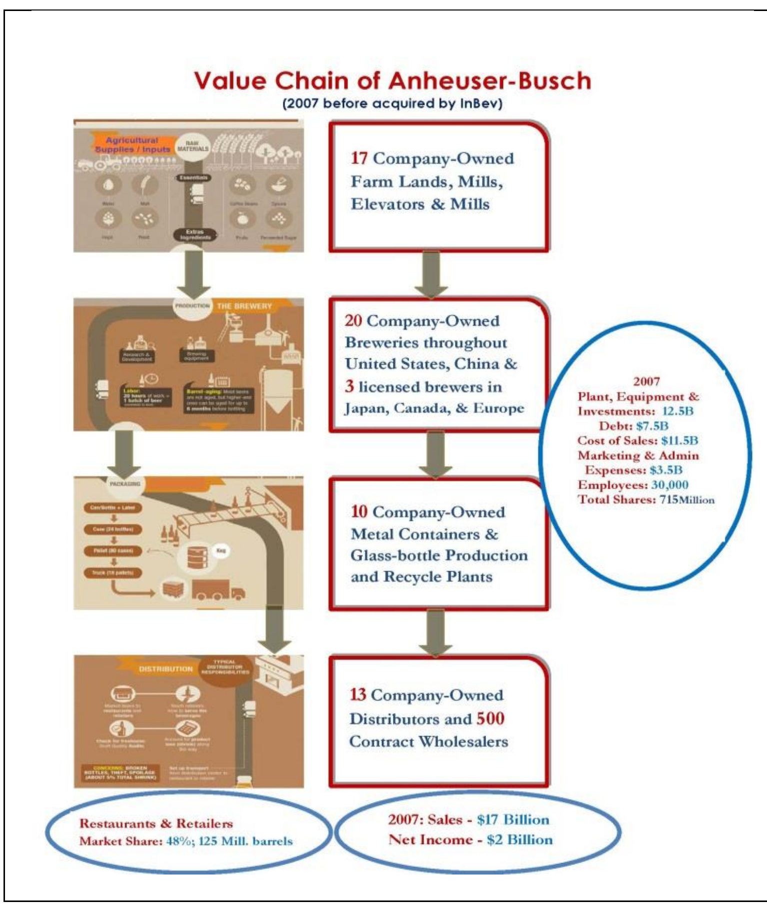
Comparison of Large Integrated Beer Firms and Firms Pursuing Smart Shoals (School of Fish Strategy)

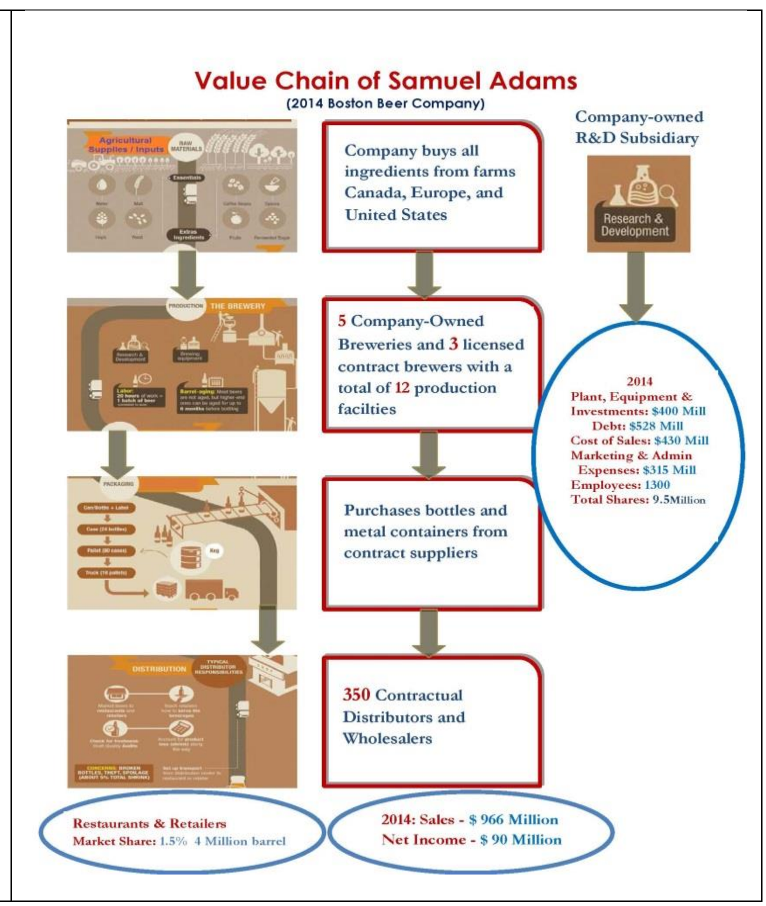
The Boston Beer Company, Inc. (SAM) 169.75 4.80 (2.91%) As of February 17 4:02PM EST. Market closed.

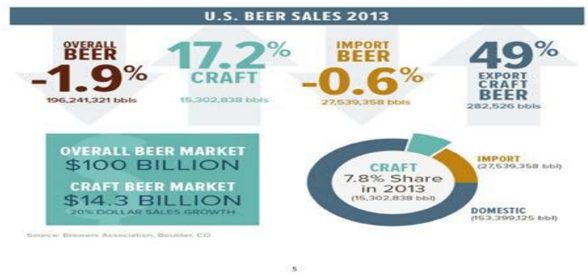
SAM Boston Beers (SAM): Constellation Brands (STZ) : Anheuser-Busch-Inbev (BUD): Molson Coors (TAP)

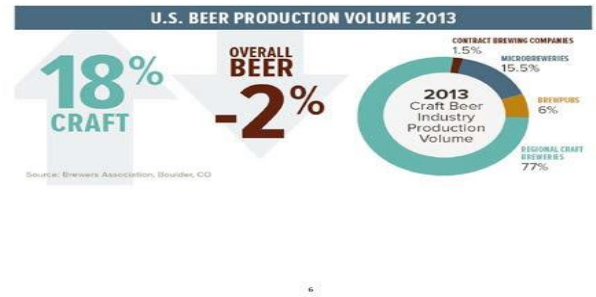
	SAM	STZ	BUD	TAP
Sales (2016)	$960 million	$6.54 billion	$42.50 billion	$4.80 billion
Net Income (2016)	$98 million	$1.05 billion	$3.94 billion	$1.97 billion
ROS - 2016	10.20%	16.20%	9%	41%
ROA - 2016	15.74%	6.57%	5.97%	9.50%
ROIC - 2016	**21.90%**	**9.20%**	9.89%	12.76%
Sales Growth (5 year)	**15.66%**	**14.49%**	**3.74%**	**6.80%**

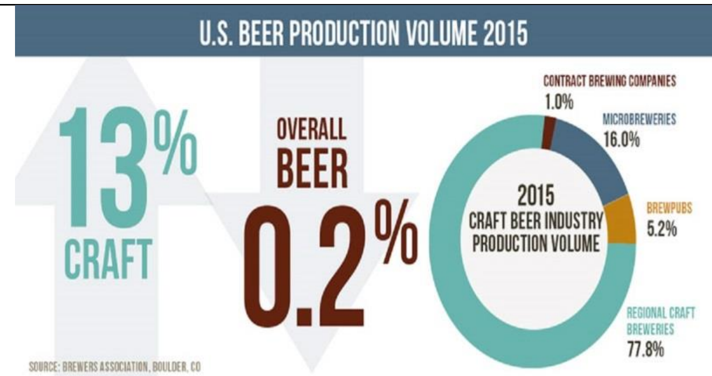
Comparison of Value Chain of Beer Companies

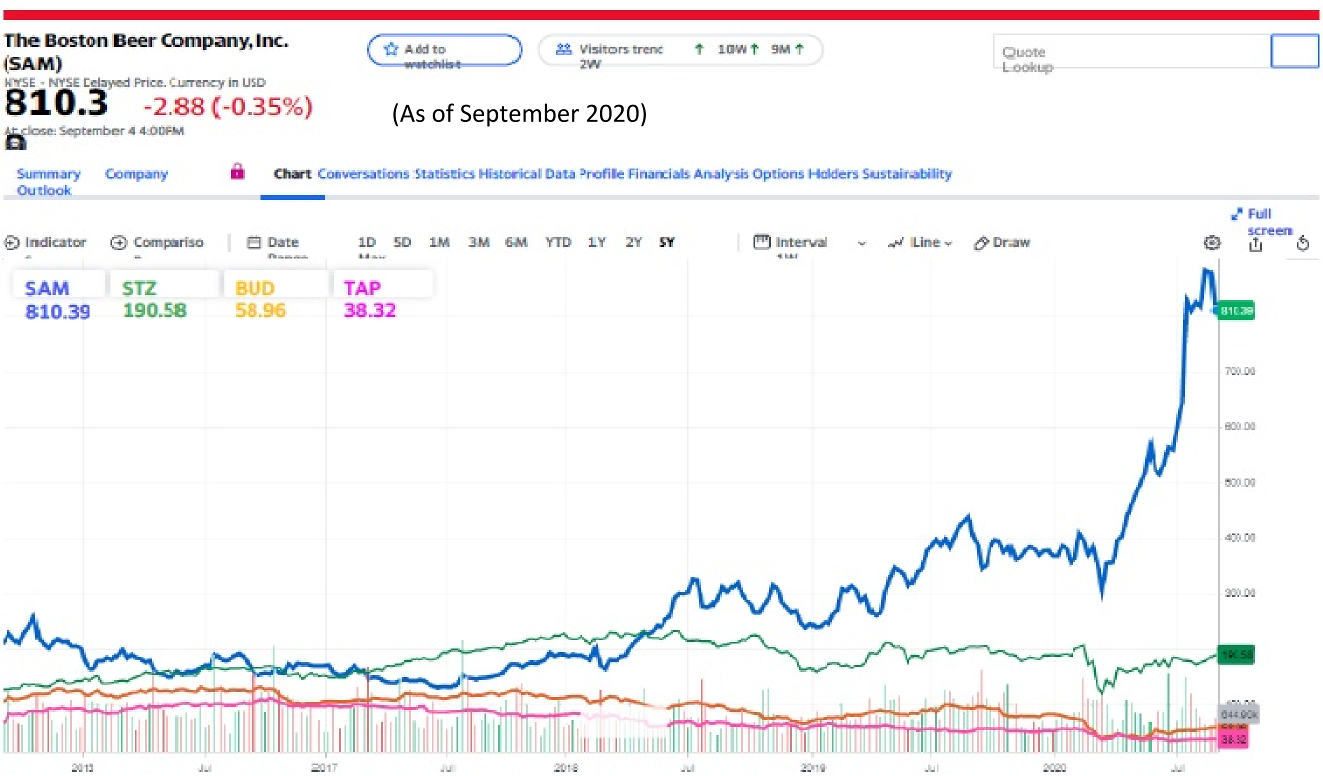












(As of September 2020)

Craft beers in the USA – breaking the industry barriers

The US beer industry totals $90 billion in sales (United States Brewers Association Statistics, 2012) and employs about 1.9 million people in the USA. The top three large-scale beer manufacturers (with production volume ranging from 6 million barrels to 125 million barrels) - Anheuser-Busch InBev (ABI), SAB Miller, and Coors - account for 80% of US market share. The recent $52 billion merger between US Anheuser-Busch and Belgian/Brazilian InBev helped the now global leader ABI to control more than 50% of beer sales in the USA. Despite high consolidation, the US beer industry has faced tough times in recent years due to a steady decline in sales volume of about 1% per year. However, in contrast, the craft beer manufacturers are growing at a rate of 10% yearly in sales and consumption volume. In 2011, the craft brewers grew by 13% in sales volume and by 15% in dollar sales, with their market share steadily rising from 1% to more than 10% of the beer market in the USA. The craft brewers include 'small and microbrewers,' with production volume ranging from 15,000 to 1 million barrels per year. According to the Brewers Association of America, there are more than 1500 craft brewers in the USA. The growth of craft brewers suggests not only a change in consumption patterns, but also a paradigm shift in the manufacturing and marketing of beer. Deregulation in the late 1970s, in combination with the craft brewers hosting innovations of flavor and quality, helped bring about beer connoisseurship (Bertsch, 1994; Carlson, 2011). The stories of two successful craft beer companies, Boston Beer Company and Sweet-Water Brewing, who are pioneering the microbrewery revolution, are presented here.

Boston Beer Company is the number one craft brewer, with a sales volume of 2 million barrels per year within a span of two decades from its inception. Founded by Jim Koch in 1985 with a family recipe, Boston Beer Company entered the market with a crafted brand 'Samuel Adams Lager.' This brand was initially brewed in small batches with an obsession for quality, freshness, and flavor. Instead of locking all their capital into production assets, Boston Beer Company has grown primarily through microbrewery production methods and contracting with third-party packers and franchisees to produce all its brands. With this shoaling approach, operating in a decentralized and dispersed chain of contract brewers, Boston Beer Company was able to market its specialty crafted beers nationally without incurring high shipping expenses (www. bostonbeer.com). The success of Samuel Adams has become an inspiration to other small and micro craft brewers.

Sweet-Water Brewing, founded by Freddy Bensch and Kevin McNerney in the mid-1990s, has its roots in Boulder, Colorado. After finishing college, Freddy and Kevin headed off to the American Brewers Guild in California - also known as Brewing School - to sharpen their knowledge of 'fermentation science.' The 1996 Summer Olympics, and the opportunities it offered, brought Freddy and Kevin to Atlanta. The friends found this town to be in need of a West Coast-style brewery that would allow them to experiment with innovations in brewing hoppy, aggressive ales. The friends named the brewery after Sweetwater Creek, a tributary of the Chattahoochee River in Georgia, and adopted the official motto Don't Float the Mainstream' as a tribute to its namesake. Sweet-Water Brewing began in January 1997, with brand names such as Sweet-Water 420. Two years later, this company hosted the 'World Beer Cup,' an international brewing competition. In 2002, Sweet Water Brewing won Small Brewery of the Year at the Great American Beer Festival in Denver, Colorado. In 2004, Sweet Water Brewing outsourced its distribution operations to United Distributors, one of the largest volume beverage distributors in the USA, increasing Sweet Water Brewing's distribution from 200,000 to 700,000 cases in six years. Now, Sweet Water Brewing is recognized as one of the top 50 craft beer brands, selling close to half a million barrels per year. The exemplary performance of microbrewers like Boston Beer Company and Sweet Water Brewing serves as a testament to the effectiveness of the shoaling strategy or the dispersed operation of manufacturing, marketing, and distribution. The success of craft brewers suggests that companies can operate profitably on a smaller scale, disaggregating their core activities to offer variety, quality, uniqueness, and customization. This strategy can effectively be replicated in a range of businesses and industries such as food processing, consumer durables, and construction to achieve innovation and growth (Carlson, 2011). Working as a band of contract brewers, bottlers, and distributors, like a ' school of fish,' craft beer sales and production in the USA have increased dramatically in the last 10 years.