

TO BREW, OR NOT TO BREW—THAT IS THE QUESTION: AN ANALYSIS OF COMPETITIVE FORCES IN THE CRAFT BREW INDUSTRY

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CASE DESCRIPTION

The primary subject matter of this case is a competitive analysis of the craft brewing industry in the U.S. The case is appropriate for courses in strategic management and entrepreneurship. The case has a difficulty level of three or four. The case is designed to be taught in 1 – 2 class hours.

ABSTRACT

This case analyzes the craft brewing industry in the U.S. It encompasses a description of what defines craft brewers, the different categories of craft breweries depending on size in the U.S. and the major competitors in the industry according to annual volume output of craft beer. Recent growth in the craft beer industry compared to the general U.S. beer industry is detailed.

In addition to craft beer brewer characteristics, the case outlines market structure, competition, and business strategies of craft breweries. Also considered are branding and social media marketing and social responsibility considerations, followed by distribution, and regulation and taxation of the craft brewing segment of the beer and beverage industry .

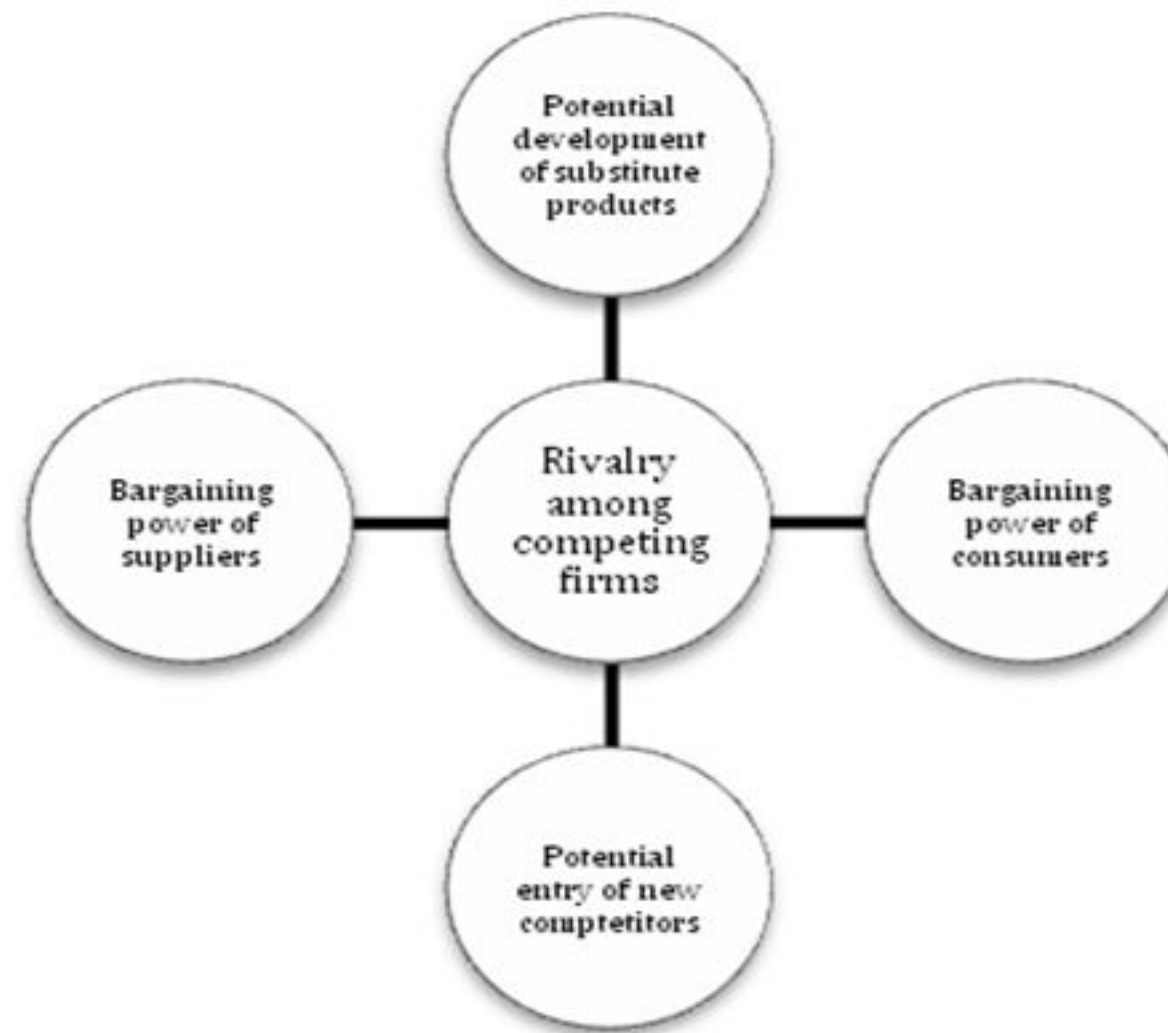
INSTRUCTORS' NOTE

ANALYSIS

Students are asked to supply answers to one instruction given at the end of the case. Additional questions/instructions could be supplied by the instructor to supplement this question as deemed necessary. The case lends itself to a rich discussion of factors (as outlined in the summary above) related to making a decision about possible entry into an existing market.

Porter's five-forces model is a frequently used vehicle to determine the nature of competitiveness in a given industry.

Porter's Five-Forces Model



Instruction: “Analyze the competitive nature of the Craft Brewing Industry using Michael Porter’s “Five Forces Model” as your guide.”

The Porter five-forces model considers the following five factors:

1. *Barriers to Entry into the Industry*--Potential entry of new competing firms is facilitated whenever the barriers of entry to the industry are low. Entry barriers could include the need for large capital investments, regulatory stipulations, intellectual property protections, technology, contractual agreements with suppliers, distribution channels or customers, availability of suitable locations, and customer brand loyalty, for example.

In the case of the Craft Brew Industry, the barriers to entry relate particularly to capital requirements, technical know-how (experienced brewmaster), and available distribution channels. In this industry, it is possible to begin with limited capital (nanobreweries) and expand production as demand warrants it. It is essential to have technical know-how to be able to create appealing brews. Therefore, the entry barriers are relatively low in this industry.

2. *Bargaining Power of Suppliers* depends upon the total number of suppliers, the ease/difficulty of obtaining substitute materials, and the cost of switching to such substitute materials. The fewer the number of suppliers and the more difficult it is to obtain substitute raw materials, the higher the bargaining power of the suppliers, and the higher the price of those raw materials is likely to be.

In the case of the Craft Brew Industry, there are a handful of large suppliers each of hops and malt, and there are two main suppliers of yeast. In this industry, the bargaining power of suppliers is high.

3. *Bargaining Power of Consumers* depends on whether customers are concentrated, large, or buy in volume. Their bargaining power represents a major force affecting the intensity of competition in the industry. Bargaining power of consumers is higher when the products being purchased are undifferentiated or standardized.

In the case of the Craft Brew Industry, customers are individual aficionados who are seeking a “taste revolution.” That is, they are enamored of the craft brew drinking experience, and, more directly, by individual brews’ tastes. These consumers tend to buy in small quantities, preferring the taste of freshly brewed beer. Therefore, in this industry, the bargaining power of the consumer is low.

4. *Development of Substitute Products* creates competitive pressures for an industry and, thereby, puts a ceiling on the price that can be charged before consumers will switch to a substitute product. The competitive strength of substitute products can be measured by the inroads into market share those substitutes can make, as well as those firms’ plans for increased capacity and market penetration.

In the case of the Craft Brew Industry, statistics indicate that major producers of regular beer have seen decreasing sales and craft brewers have gained volume. However, with the recent legal revision of the upper limit volume from 2 million to 6 million barrels to still be classified as a craft brewer, the stakes have changed for the major producers of regular beer. They may now be interested in acquiring craft brewers or starting their own craft brewing operations. This will likely increase the rivalry among all craft brewers.

5. *Rivalry Among Competing Firms* is usually the most powerful of the five competitive forces. That is so because strategies that have proven to be successful for one competitor are often quickly adopted by other competitors seeking to level the competitive playing field. Example Gas Price Wars: One gas station in a given neighborhood lowers the price of its gasoline to attract new customers. It is likely that in very short order his competitors will lower their prices to his new price or respond with an even lower price, which could in turn result in a retaliatory spiral by others until all competitors realize that they are playing a “no win” game. Behavior like this was quite common in the U.S. at one time. Retaliatory moves by competitors can extend not only to price but to other issues such as, for example, product features, quality enhancements, terms and conditions of sale, and advertising as well.

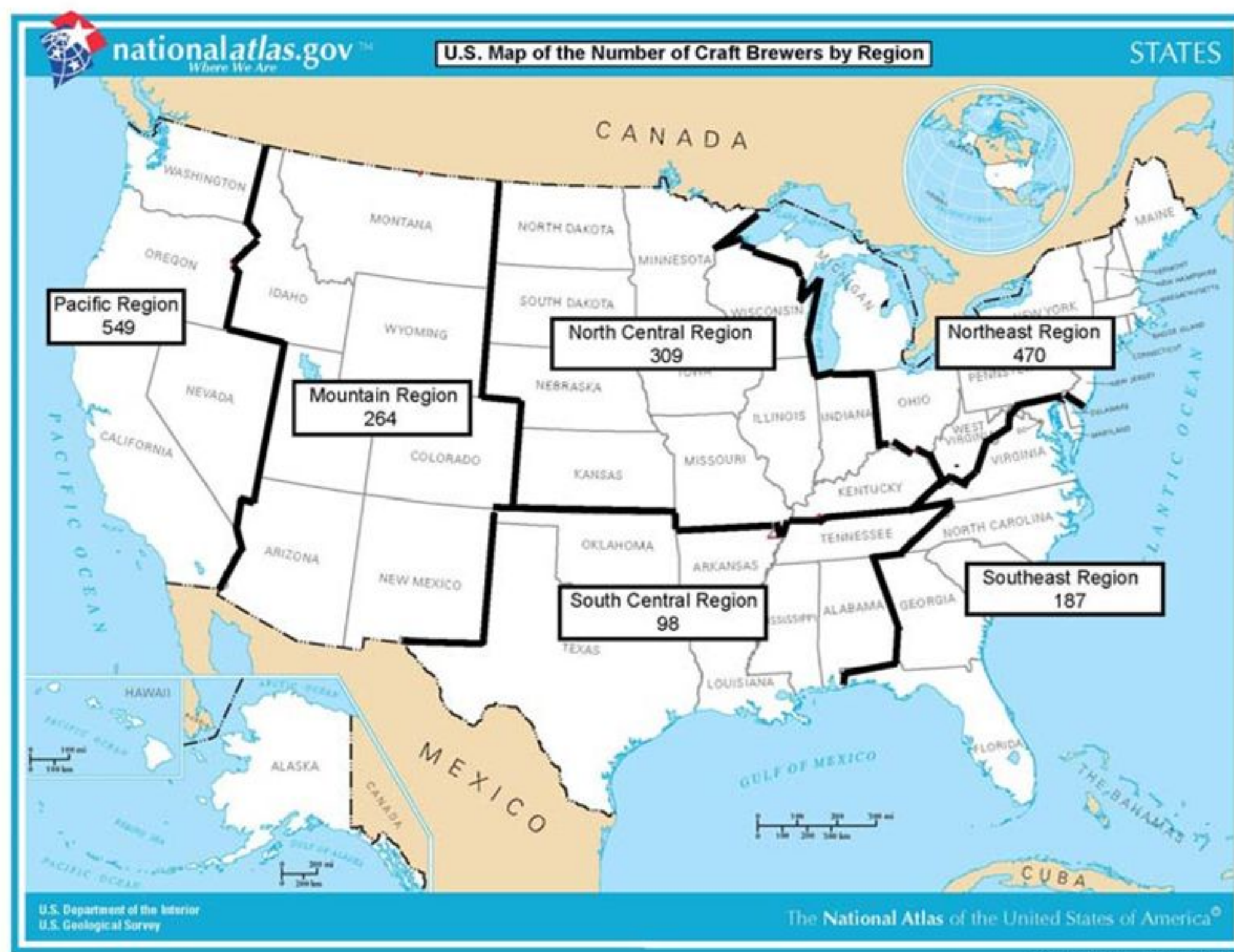
The intensity of rivalry among competing firms in an industry is influenced by:

- a. the number of competing firms
- b. the more equal in size and capability (power) the firms are
- c. the demand for the industry’s product increases or decreases
- d. the ease/difficulty with which consumers can switch to other brands
- e. the ease/difficulty with which firms can enter/leave the industry

- f. the level of fixed costs
- g. the extent to which the product is perishable
- h. the diversity of strategies employed by competitors
- i. the extent of merger and acquisition activity in the industry

As rivalry among competing firms intensifies, industry profits decline to perhaps the point where an industry becomes inherently unattractive. In cases like this, new firms entering such a market would find themselves struggling not only with already low profits but also hostile behaviors by existing firms attempting to protect their customer base, which would likely lower profit margins even further.

In the case of the Craft Brewing Industry, there appears to be limited competition at this time. However, as detailed in the *Substitute* section, there was a recent modification (January 2011) in the law applicable to craft brewers. The new law allows brewers to produce up to 6 million barrels and still retain their classification of craft brewers, which is a differentiating and valuable moniker in the market place. The larger volume (coupled with the higher profit margin of the craft brew industry) may make entry into this brew category more appealing to the majors, thereby potentially increasing competition in the craft brew segment.



YOUTUBE CRAFT BEER INDUSTRY VIDEOS

THE CRAFT BEER INDUSTRY

- History Channel Series: Beer Documentary-5 part series
http://www.youtube.com/watch?v=_DbPUtXtudE&feature=related
 - It's the most popular beverage on the planet - mankind's first recipe carved in stone ten thousand years ago, and today, beer still rules. The history channel journeys to find the timeless secret to beer's magic: how it's made, how it's marketed, how new beers are invented and tested and how the giants jockey for global supremacy.

- Allagash Beer - Interview with Brewmaster Rob Tod
<http://www.youtube.com/watch?v=uu6MP8xYMZc&feature=relmfu>
 - Meet Allagash Brewery owner and Brew Master Rob Tod up at American Flatbread in Burlington, VT, during an annual Allagash beer shindig. He shares some history of the brewery and future outlook.

- Maine Beer Company - Portland Maine
http://www.youtube.com/watch?v=q0Igw3_obc0
 - Maine Beer Company is a very small microbrewery located in Portland, Maine. They don't concentrate on any particular style of beer. We don't do just big beers or small beers or light beers or dark beers. Our production is limited and our process is slow (our beers are 100% bottle conditioned) but our dedication to brewing really good beer and doing what's right always comes first.
 - http://mainebeercompany.com/About_the_Trainer.html

- Anchor Brewing Company: A conversation with craft beer pioneer Fritz Maytag
http://www.youtube.com/watch?v=0zc4p9Uwa_s
 - Fritz Maytag, longtime owner and brew master of the Anchor Brewing Company, is a central figure in the story of the American craft beer revolution. When Maytag bought Anchor Brewing Company in 1965, he blazed a new trail in the beer industry. At a time when the market was increasingly dominated by big breweries selling inexpensive, watery lagers, Maytag decided to devote his life to creating more flavorful and traditional beers.

- Dogfish Head Bitches Brew | Craft Beer Review
<http://www.youtube.com/watch?v=2m0jnlwDWvA>

- Marcus Guiliano, Chef and Owner of Aroma Thyme Bistro located in Ellenville, NY in the scenic Hudson Valley. Aroma Thyme is known for their "stealth health"(Zagat). The Bistro has an award-winning wine list from Wine Spectator Magazine and over 200 beers. Aroma Thyme is certified green by The Green Restaurant Association.

CRAFT BEER INDUSTRY GROWTH

- "I Am A Craft Brewer"

<http://www.youtube.com/watch?v=ev5OZS75qaY>

- A collaborative video representing the camaraderie, character and integrity of the American Craft Brewing movement. Created by Greg Koch, CEO of the Stone Brewing Co. and Chris & Jared of Redtail Media...and more than 35 amazing craft brewers from all over the country. The video was shown to a packed audience of 1700 craft brewers and industry members at the 2009 Craft Brewers Conference as an introduction to Greg's Keynote Speech entitled "Be Remarkable: Collaboration Ethics Camaraderie Passion."

- Brewpot.com interviews Paul Philippon Brewmaster of The Duck-Rabbit Craft Brewery

<http://www.youtube.com/watch?v=I1MgoFqg5GI&playnext=1&list=PL7E484421D5AAF404>

- Brewpot.com Craft Brewers Conference Interview Series
- Paul Philippon
- Craft Brewers Conference
- Boston, MA
- 20th-24th April, 2009

- Earnings Report: The Boston Beer Co. (NYSE:SAM) Misses Estimates, Top Line Up 3%

<http://www.youtube.com/watch?v=jaot-tYhX8o>

- The Boston Beer Co. (NYSE:SAM) reported Q4 EPS of 52 cents, missing consensus estimates of 58 cents. Revenues for the quarter rose 3% year-over-year to \$107.2 million, falling short of consensus estimates of \$110.83 million. For 2010, the company expects EPS in the range of \$2.35 to \$2.65, versus consensus estimates of \$2.47.

- Craft Beer Culture

http://www.youtube.com/watch?v=q-4FU0cf_VU

- Craft brewers around the nation are reporting big gains in the first half of 2010. I went over to the Craft Lager Fest in Manitou Springs and spoke to some breweries to see why craft beer's popularity continues to grow.

THE CRAFT BEER BREWING PROCESS

- How is Beer Made? The Brewing Process
<http://www.youtube.com/watch?v=Ycnwc5vPaAo>
 - Have you ever wondered how beer is actually made? In this video, featuring Daniel Kahn of Buckbean brewing company in Reno, NV you can learn all about the brewing process, including specifics on the importance of many of the elements that go in.
- Beer Brewing with Fritz Maytag: Anchor Brewing Co. | Pottery Barn
http://www.youtube.com/watch?v=zs4nIUsJ_ps
 - Get an inside look at the art of beer brewing, as Fritz Maytag, owner and master of Anchor Brewing Co, explains the process that goes into producing quality beer. Not only does Fritz reveal how to make beer but also how to incorporate beer into any outdoor party planning ideas.
- How to Brew Ale Beer : Tips for Brewing Award-Winning Beer: Part 1
<http://www.youtube.com/watch?v=U8WjtnHgNzo>
 - Learn tips and techniques for home brewing award-winning beer with expert beer tips in this free home brewing video clip. Expert: Eddie Leal Bio: Eddie Leal is an award winning Master Brewer at the Steelhead Brewing Company in Irvine, California. Filmmaker: Joseph Mann
- How we make organic beer at Orlando Brewing
<http://www.youtube.com/watch?v=rj1v5g8rejg>
 - Ed Canty the Brewmaster explains the organic brewing process at Orlando Brewing.

THE CRAFT BEER INDUSTRY VALUE AND SUPPLY CHAIN

- Public Hearing Feb 8, 2011 - Part 1
<http://www.youtube.com/watch?v=oM-j7tSwMVQ&feature=related>

- Connecticut's five breweries and several of the state's brewpubs and other beer related companies have come together to promote the local craft beer culture through a new social media website which enables beer fans to virtually connect with their favorite beer producers and each other. The web site's launch comes at a very interesting time for Connecticut beer as local legislators introduce a new bill, which, when passed, will establish official state support for the development of the CT Beer Trail.

TYPES OF CRAFT BEER COMPANIES

- What is a NanoBrewery?

http://www.youtube.com/watch?v=Qsa3agRVh_Q

- More beer history for you, *What is a NanoBrewery* explores a new concept of brewing beer. The specifications define how to be licensed and more.

- How to Brew Ale Beer: Brewpubs Vs Microbreweries

<http://www.youtube.com/watch?v=D9xmODfwaJ8&feature=fvvr>

- Learn the differences between brewpubs and microbreweries with expert beer tips in this free home brewing video clip.