TOPIC: SUPPLY CHAIN

KEYS TO SUCCESSFUL CONTRACT BREWING

7 min read

In the Oxford Companion to Beer, Editor-in-Chief, Garrett Oliver, defines contract brewing as, “an arrangement where a company brews and packages beer on equipment it does not own.” While this is a simple, straightforward definition, it becomes more complex when you consider the fact that for a contract brewing arrangement to be successful, it needs to be mutually beneficial for both the contract brewer and for the client.

For the client, there can be several reasons why a contract brewing arrangement would be a good option for your success. One reason could be the avoidance or postponement of capital investments needed to install added capacity. For instance, you may wish to first develop your brands and scale up quickly while you explore longer-term potential in various geographical areas. Another reason could be the fact that your own brewery's capacity has maxed out much sooner than anticipated and a rapid response for added capacity is needed.

For the contract brewer, there can be several reasons for getting into this business model. In some cases, it may be that your entire business model is based on contract brewing for clients. Alternatively, you may see this as an interim phase in your business model that may only last a few years, until your production capacity is fully utilized with your own products. Filling up your excess capacity, if done right, will help bring costs down for your own products as some of the fixed costs will be spread over a larger volume produced, for instance.

As an example of a successful contract brewing case, Oliver describes how the Boston Beer Company used the contract model to successfully brew Sam Adams Boston Lager. The contract brewing approach "helped to establish and solidify the American craft beer movement in the 1980s." Almost 45 years later, that model is still widely in existence. Which brings us to the essential question of this article: What does it take to be a successful contract brewer?

Consider the Future Possibilities…and the Current Realities

For breweries with excess capacity who are considering contract brewing, it is important to fully understand your current capacity as well as your future capacity needs. Through a strategic planning process, you can envision how this contract brewing option will work in practice in the short, mid, and long-term. Questions such as:

- How much capacity is available, and under what assumptions? It is important to keep in mind that the clients' recipes and processes might be considerably different than the brewery's current product portfolio. For instance, the fermentation or maturation times will impact the actual cellar capacity available in a disproportionate way if the client's product requires a long aging time. Likewise, the minimum batch size the contract brewer is willing to produce will also have an impact on capacity and costs (consider, for instance, the case where one faces the use of partially-filled tanks, and the reality of very short packaging runs). Capacity aspects should include the entire brewery, from ingredients to packaged product, to warehousing and utilities.
- What resources will be needed to effectively manage contract brewing arrangements? Here you can think of the resources needed to find clients, and the resources required to effectively manage communication and coordination with the clients. For instance, do you already have a potential client list ready to go or will you need to develop a list? What competition will you have? What laboratory resources and quality management requirements will likely need to be met and is the contract brewer staffed to fulfil these?

As consumer preferences are constantly changing, brewing and beverage facilities that can offer high quality, innovative product solutions such as non-alcoholic beers, seltzers, RTD cocktails, energy drinks and functional non-alcoholic beverages are all in demand.

Know Your Costs

It is important to consider the fixed and variable costs, and depending on what the contract encompasses, the distribution costs as well. There may be some procurement advantages from the larger volumes produced (although this may not be the case if the contracted volume utilizes primarily unique materials and ingredients not in use in the other products produced). It is also important to consider situations where added utilities might be required beyond what is currently needed (e.g., utilities involved when using an alcohol removal unit). Another important aspect of knowing your costs is anticipating what the expected process yields might be, as some recipes will result in higher product losses. Likewise, very short packaging runs may result in excess product that has to be disposed of in a mutually agreed upon manner.

Knowing your costs will ultimately give you another important financial measure – your desired profit margin. "Just because you grow volume, this doesn't mean you'll be more profitable," says Scott Durnin, a senior advisor at First Key – a helpful reminder to keep in mind as you consider contract brewing.

Get the Team's Input and Buy-In

Involve all parties in early discussions about how the proposed contract brewing arrangement will work in practice. Make sure to include especially those who will be responsible for managing the contract brewing relationships. Whether you're a large or small brewery, team members can provide very important insights whether it is on the procurement, brewing, packaging, utilities, quality and warehousing aspects. Some of them will need to be designated as responsible for managing the day-to-day communications with the clients. It's important to uncover potential risks, anticipate problems and look for opportunities that can sometimes make or break a deal.

Define Your Customer Service Plan

Michael LeBoeuf, author of many successful, internationally published business books, says, "A satisfied customer is the best business strategy of all." Breweries who are in contract brewing arrangements must satisfy the clients they're brewing for. And that begins with having solid communications even before the formal agreement is signed.

A designated employee, such as the Director of Brewing Operations, will need to be in direct communication with the contract brewing client. In some cases, there may be multiple people designated for specific communications (e.g., production, laboratory, scheduling, etc.). It is also important to anticipate how exceptions will be handled, e.g., what will the escalation process look like if there is a production issue or a quality control problem? How will decisions be made and communicated under such circumstances?

Establish Quality Specifications

It is critically important that the success metrics include well-defined quality specifications that are well-understood and agreed upon. Which key parameters will be measured? What will the sampling plan consist of? What are specification limit ranges? This includes chemical, microbiological, physical and sensory metrics throughout the process and on the packaged product. How will the client be involved in data review, product tasting, product disposition decisions when one or more parameters are outside the acceptable range? How will consumer complaints be handled?

Establish a Good Contract

A well-drafted contract that outlines all the terms and conditions of the arrangement is essential and can help prevent many headaches later. It should include details about the beer or beverage recipes and specifications expectations, the production volumes anticipated and the mechanism to adjust these numbers with a defined realistic lead time. The contract will also include the procurement arrangements, the inventory management policies (and distribution arrangements if applicable), the pricing, payment terms, intellectual property rights, conflict resolution mechanisms, and termination clauses. Legal advice is often recommended to ensure that both parties are protected and that the production facility and the products produced meet all necessary regulations. The contract should also spell out the arrangements needed for the initial test production: what costs will be covered by the client? What disposition will be given to the test product produced? If added equipment will be needed (e.g., color-removal or alcohol removal units), who will pay for the equipment, its installation and commissioning, and what will the ownership of that equipment will be? Will the equipment be used exclusively by one client, or can other future clients use that equipment?

When asking successful contract brewers what has enabled them to be successful, they mentioned many of the factors covered in this short summary. They highlighted a few for us: having clear communications, having well-defined quality standards, and a willingness to work together, adjusting and adapting when unforeseen circumstances arise. Perhaps this last point cannot be overemphasized: long-term successful contract brewing happens when both the contract brewer and the client are indeed successful.

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