



TOPIC: SUPPLY CHAIN

TRANSPORTATION: HOW TO WIN IN BEER IN THE FUTURE

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Market consolidation is happening across manufacturing, wholesaling, and retailing in the beer industry. In 2022, the U.S. Treasury Department studied the problem of market concentration and competitiveness in the industry and found that state alcohol laws can often favor large producers. This may be unsurprising since many of these laws date back to a time before craft beer became a relevant force in the overall beer industry. Therefore, craft breweries must operate within a system that puts them at a competitive disadvantage in getting their products to market efficiently and at a manageable price.

The major threat facing the overall beer industry in terms of the supply chain is inflation. The COVID pandemic in 2021 and 2022 resulted in overall U.S. inflation hovering at levels not seen in the prior 40 years. The beer industry exceeded the overall inflation rate, reaching 7.7% in 2022. According to the Consumer Price Index (CPI)[1], the inflation rate for beer was well above other alcohol categories, with whiskey at 1.7%, wine at 3%, and other spirits at 1.7%. Beer was specifically impacted because of the effect of climate change on barley and hops, energy market increases and higher raw material costs in CO₂, and aluminum cans. There is also the effect of ongoing labor shortages persisting in the U.S. and other industrialized nations due to age demographic changes that will linger with no end in sight. These inflationary effects on raw materials and labor are relative to all beer producers, and other alcohol brand categories of course. However, the larger beer producers benefit from economies of scale and other mechanisms not in place for craft producers.

Core strengths of the craft brewer segment include a strong focus on differentiation: wide ranging, innovative flavor profiles and a variety in package and container formats and sizes. These all contribute to fierce customer loyalty. However, an influx of new products and hybrid drinks from outside of the beer industry (i.e., wine, spirits, cannabis, and soft drink producers) have taken focus away from the innovation normally generated by craft brewers. Other headwinds have included a shift to lower alcohol drinks and non-alcoholic products. For craft breweries to survive they must operate profitably and in addition to their core strengths, an understanding of how to win within the beer supply chain and distribution system is crucial.

How will craft brewers succeed within the current distribution model?

1. **Understand transportation spending and its impact on current and future financials.** In our experience, a craft brewer's fully loaded transportation costs per unit can be as much as twice that of a large brewer. As a rule of thumb in the consumer products industry, transportation costs before COVID were 6-8% of the cost of goods sold (COGS). Today, the transportation market is stabilizing for large shippers who have strategic managed freight programs with freight providers, but not for those without a strategy. This includes many craft producers, and they continue to face higher prices and more volatility.
2. **Understand how freight pricing can be managed** by factors such as optimizing the origin-destination pair to market conditions and ensuring service through service level agreements, freight billing and other crucial factors. In many cases, brewers are paying up to a 25% premium without understanding real market rates and the attendant hidden costs. Jack Buffington, Director of Supply Chain and Sustainability at First Key Consulting says, "We have seen immediate ROI on transportation and supply chain reviews in client projects which shows the opportunity for craft brewers to become more profitable".
3. **Develop a transportation strategy** and the tactics and practices that support this strategy. A stable transportation strategy will limit exposure to higher costs and maintain desired service levels with wholesalers and retailers.
4. **Once the craft brewer has a transportation strategy, find strategic freight partners that can help them achieve these objectives.** Many transportation companies offer a strategically managed freight program focusing on the larger brewers for obvious reasons but may also be willing to partner with those mid-sized and smaller craft breweries with a developed strategy. Such partnerships can lead to lower costs and market growth potential for the craft brewer. Working together, pro forma analysis can be developed to demonstrate how costs can be reduced and market share can be increased.

All these suggested activities will not only generate cost reductions and growth opportunities in the current distribution models, but they will also prepare craft brewers for the future.

Future Opportunities

Opportunities for craft brewers will emerge along with the potential development of e-commerce ordering and fulfillment as well as direct-to-store (DtS) delivery. From 2010 to the end of 2019, e-commerce in the U.S. grew from 4.2% of retail sales to 11.2%, and then surged due to COVID in 2020 to over 15%. In the beer market, e-commerce sales are less than 1% given the state regulatory laws, but this will change with potential state deregulation of the beer industry. E-commerce and DtS would be the most significant opportunity for craft beer since its broad-based inception in the 21st century.

Craft brewers can only take advantage of these opportunities by moving away from a model that has made them successful over the past decade. While many brewers will naturally gravitate towards their core expertise, the reality is that the game is being won and lost in the approach to the supply chain. Craft brewers must build a new model for growth that leverages the evolution we will see in the distribution and retail markets.

In neither the current distribution model nor the future model should craft brewers try to be all things to all potential retailers and consumers. Craft brewers must know:

- the consumer segment being targeted.
- their brand personality and how to establish and support this identity online.
- their desired pricing range.
- their competitive set and how to make their brands stand out within that set.
- the retailers that understand and serve the consumer target group.
- marketing and support opportunities available at retailers.

Craft brewers must build a new model for growth to focus on winning in the future!

[i] Mike Snider (2023). "Is beer getting more expensive? Prices up more than groceries and people are buying fewer brews."