



BroadBranch Advisors

Growth opportunities for non-alcoholic craft beer in the United States

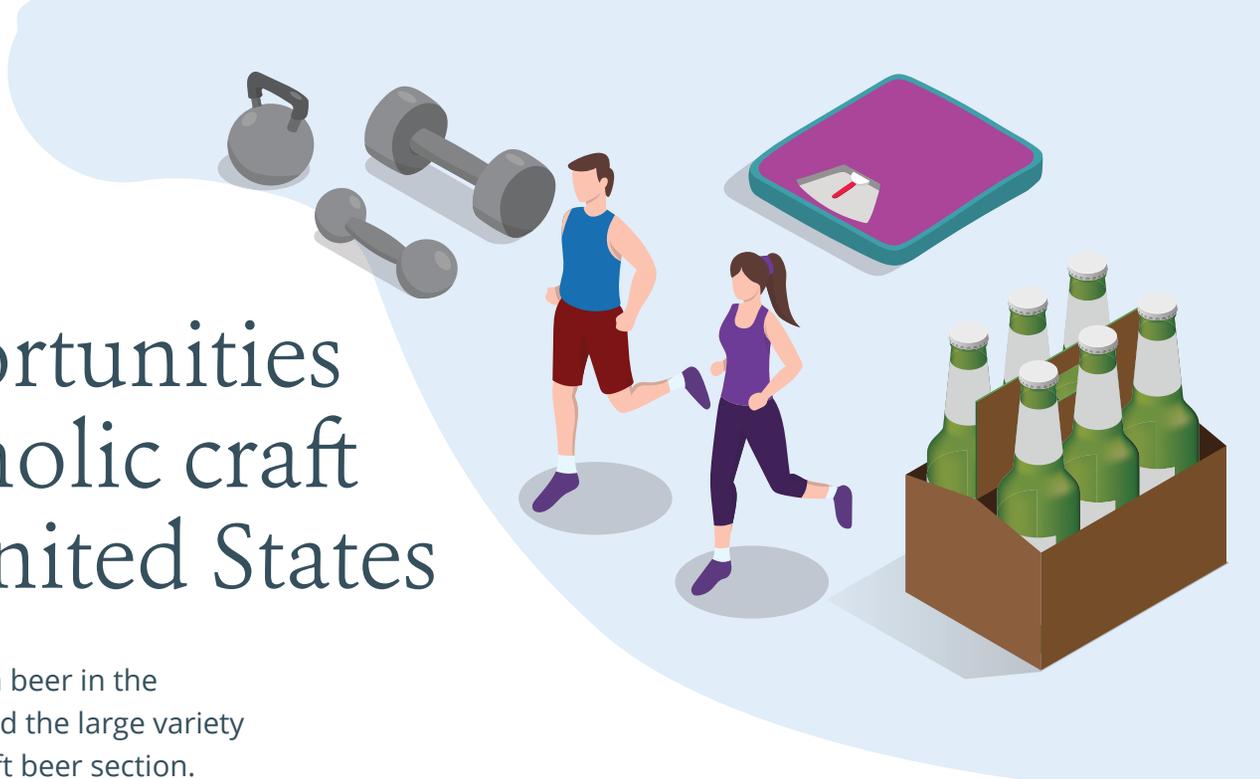
Anyone who has recently tried to buy a beer in the United States will probably have noticed the large variety of beers available, especially in the craft beer section. Craft breweries, defined as any brewery that produces less than six million barrels per year and which is mainly independently owned, have seen a dramatic increase since the early 1980s.

In addition to the rise of craft breweries, another trend in the brewing industry has recently emerged: the growth in the number of non-alcoholic beers offered. Non-alcoholic beers have suffered a sad but often justifiable reputation

The growth potential for this niche is not to be understated as the market for non-alcoholic beers grew by 31% from 2020 to 2021.

as a tasteless and undesirable alternative to 'real' beer. This perception, however, is changing. Large breweries like Heineken or AB InBev have launched non-alcoholic beers with positive results. The growth potential in the United States for this niche is not to be understated, as the market for non-alcoholic beers grew by 31% from 2020 to 2021. Despite this growth, the share of non-alcoholic beers in the US held an almost negligible share of the \$94B US beer market. For comparison, in Europe, the consumption of non-alcoholic beer represents about 10% of the total beer market, indicating a possible growth potential in the US market as consumer patterns change.

After analyzing the non-alcoholic beer market and speaking with industry experts, BroadBranch Advisors believe that there is an opportunity for craft breweries to





This shift to non-alcoholic alternatives does not mean that consumers want to abandon the social aspects of beer-drinking culture. After almost two long years of lockdowns and isolation during the COVID-19 pandemic, consumers are yearning to interact again in social environments.

expand their consumer footprint by offering non-alcoholic craft beer. We believe that direct-to-consumer distribution through e-commerce or on-site sales offers the most straightforward entry into the market. Furthermore, smaller craft breweries should consider using non-alcoholic brewing methods (e.g., arrested fermentation), which bypass legal complexity and heavy initial investment into specialized equipment.

Changes in Consumer Patterns

Many consumers are increasingly emphasizing healthier lifestyles in all aspects of their lives, driving increased demand for a variety of healthier alternatives to traditional products, including beverages. Movements like “Dry January” (a pledge to abstain from alcohol during January)

have gained popularity, especially after the COVID-19 pandemic, where many consumers found themselves over-indulging in alcohol. In addition, the potentially damaging effects of alcohol are becoming more evident to consumers, evidenced by a continuous downward trend of per-capita alcohol consumption over the past decades.

While the demand for alcoholic drinks has decreased, the demand for alternatives to alcoholic beverages (e.g., Kombucha, mocktails, and of course, non-alcoholic beers) has increased rapidly. For example, Athletic Brewing, a craft brewery exclusively producing non-alcoholic beer, has successfully targeted the active lifestyle market by introducing consumers to non-alcoholic beer at sporting events. “Although the ingredients for beer do offer health benefits, alcohol nullifies these,” mentioned a craft beer industry expert. He continued, “non-alcoholic beer straddles the gap between enjoying flavorful beer and being health-conscious.” A beer buyer we spoke with mentioned, “I don’t drink beer to get drunk. I drink it for the flavor and social experience”.

This shift to non-alcoholic alternatives does not mean that consumers want to abandon the social aspects of beer-drinking culture. After almost two long years of lockdowns and isolation during the COVID-19 pandemic, consumers are yearning to interact again in social environments. Beer culture, which is engrained in the United States, plays a significant role. A brewer for Sierra Nevada Brewing Company, the second-largest craft brewer in the United States, sums it up: “Beer is a social beverage. Drinking beer for me is all about the company I keep while I am



drinking". Brewpubs and taprooms offer social meeting spaces where consumers can enjoy a unique, and in terms of craft-breweries, hyper-local experience. Non-alcoholic beverages offer consumers who do not wish to drink alcohol the ability to participate in the social aspect of beer culture. An expert on craft brewing defined the social aspect as "a desire for us humans to belong and not feel like an outcast. Non-alcoholic beers allow craft breweries to cater to a widening customer niche, and we are very supportive of that".

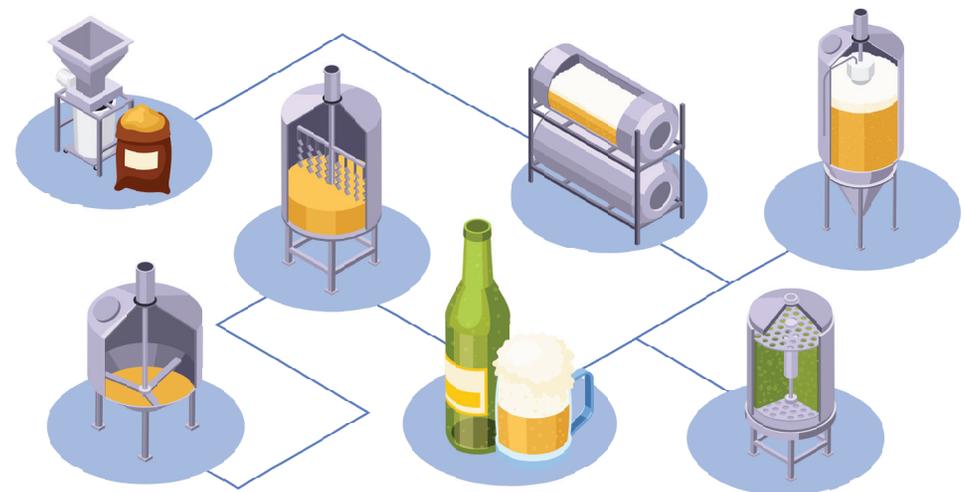
Choosing the right brewing technique

It may seem logical and straightforward for craft breweries to offer a non-alcoholic alternative. However, brewing non-alcoholic beer comes with its unique challenges. Craft brewers have to choose which method to use when brewing non-alcoholic beer. Depending on the process used, either the TTB (Alcohol and Tobacco Tax and Trade Bureau) or the FDA (Food and Drug Administration) will be responsible for the regulation.

The most common method used is vacuum distillation, which produces consistent non-alcoholic beer. The beer is brewed like regular, alcoholic beer, after which the alcohol is removed through a vacuum distillation process. This added step makes the production of non-alcoholic beer more complex and therefore more expensive. Craft brewers who decide to use this brewing method will

have to consider the high initial capital investment needed to obtain the distillation equipment. Finally, even though the alcohol is removed from the beer, the mere fact that alcohol is produced in the first place can result in tax implications for the craft brewer (not to mention the possibility of additional licensing needed for distillation equipment). "The moment yeast hits sugar and fermentation begins, you may be liable to be taxed," warns an industry expert. Breweries can reuse the removed alcohol in other beverages, such as hard seltzers, and as a result, the option to use vacuum distillation may be most attractive to larger craft breweries that can shoulder the initial investment burden for equipment and who already might be producing other alcoholic beverages.

For smaller brewers of non-alcoholic beer, the arrested fermentation method offers a cheaper production method. On a high level, arrested fermentation involves brewing beer without creating alcohol by using special





yeasts and malts. Craft breweries that use this method bypass the implications of producing alcohol entirely. Non-alcoholic beers produced through arrested fermentation can have a sweeter and less “beer-like” taste profile which may not appeal to all consumers. Craft brewers must also be careful to avoid the possibility of beer re-fermentation, which may occur if the beer is improperly packaged.

The good news for non-alcoholic beer aficionados is that craft brewers seem to share the enthusiasm and revel in the challenge of making a good, flavorful non-alcoholic beer. When challenged about the legitimacy of non-alcoholic beer, a brewer from The Boston Beer Company stated that “non-alcoholic beers are absolutely beer. The ingredients are still the same. Making a flavorful non-alcoholic beer can be challenging. There are many factors you need to consider to create a taste as close as possible to alcoholic beer. I enjoy that challenge.”

Distribution is key

The brewing of non-alcoholic beers is one thing but as any craft brewer will know very well, distributing the beer to the end consumer is a different challenge altogether. To succeed in launching a non-alcoholic

beer, craft breweries need to play to their unique strengths and exploit any advantage the non-alcoholic nature of their products can add in reaching customers more efficiently.

Unlike Europe, where breweries can sell directly to retailers, the beer industry in the United States is subject to a three-tier distribution system. Any

beer must go through the hands of a distributor before retailers can sell it. “For a craft brewery, using distributors is a mess,” an independent beer consultant noted. Beer distributors are highly fragmented, and larger distributors often hold lucrative exclusivity agreements with major breweries, making it difficult for new market entrants to sell their products. Furthermore, shelf space at retailers is limited, and retail category managers work closely with distributors to plan their inventory

for the following retail cycle. Even though non-alcoholic beer may not require distribution through an alcoholic beverage distributor, retailers still rely on separate non-alcoholic beer distributors to fill their shelves. As part of our research, we spoke to a beer and wine category manager working for a national retailer to understand these constraints in more detail. “A brewer can have all the relationships they want with retailers, but if they don’t have a good relationship with distributors, their product isn’t going anywhere.



If you call me up outside of my planning cycle trying to make me stock your beer, all I can say is, 'tough luck.' I am not going to sell your product until the next cycle." Based on these challenges, it becomes clear that any craft brewery wishing to sell their non-alcoholic beer through traditional retail channels must work closely with smaller regional distributors who are not bound by exclusivity agreements to understand retailer inventory cycles.

Instead of relying solely on traditional distribution methods, craft breweries should exploit two unique advantages that non-alcoholic beers and their market niche offer them. First, craft breweries often offer local meeting spaces with food and entertainment where their beer can be consumed on-site. They frequently become destinations in their own right. These spaces cater directly to the social aspect of beer culture highlighted earlier. Most importantly, craft breweries can bypass distributors directly because their beer is sold on-premise. This go-to-market strategy has several advantages. Untouched by distributors and retailers, on-premise sales to end-consumers result in a significantly higher profit margin for craft brewers. On-premise sales also enable the craft brewery to cater to a unique consumer experience.

The second advantage for brewers of non-alcoholic beer is that their product opens up a previously closed distribution method: e-commerce. Due to its nature, non-alcoholic beer does not fall under the same, often stringent, regulatory requirements as alcoholic beer. As a result, interstate, direct-to-the-consumer shipping is possible, as your author found out by sampling many brands of non-alcoholic beer from his home (e.g., Athletic Brewing, Partake Brewing, Rightside, Hairless Dog Brewing). Craft breweries can use this opportunity to transform their often hyper-local brands into brands with a nationwide consumer footprint.

As we spoke to industry experts and brewers, one message was repeated: non-alcoholic beer is here to stay and the market will continue to grow. "The market is still in its infancy. Non-alcoholic adult beverages are on the rise and many brewers are shifting from a beer company to a beverage company," says an R&D brewer for a non-alcoholic craft brewer. Taking into account rapidly changing consumer behavior, different production techniques for non-alcoholic beer, and unique go-to-market aspects, craft breweries have an opportunity to become important players in the non-alcoholic beer space, provided they make careful decisions on production and distribution methods.

Please contact Julian Fietzek for more information.



Julian Fietzek

Senior Associate

julian@brbradv.com

+1 703-819-9070



B R O A D B R A N C H
A D V I S O R S