TRILLIUM NETWORK
FOR ADVANCED MANUFACTURING

Good Things Brewing: Ontario's Craft Beer Industry, 2010-2019

JUNE 2020

BRENDAN A. SWEENEY

Introduction

In downtown Toronto or the small towns that dot rural Ontario, it is increasingly difficult to find a community without a local brewery. From Kenora to Vankleek Hill, and Windsor to Haileybury, breweries, which exist at a unique intersection between manufacturing, agri-food, tourism, retail and hospitality, play an important role in local economies and as community hubs.

In the past decade, employment in breweries—on a proportional basis—grew more than any other segment of provincial manufacturing.

In the past decade, employment in breweries—on a proportional basis—grew more than any other segment of provincial manufacturing. The number of persons employed in Ontario breweries increased from approximately 2,220 in 2010 to more than 5,800 in 2019. This growth did not occur equally across the industry. Employment in Ontario's internationally-owned breweries decreased slightly between 2010 and 2019, while employment in Canadian-owned breweries increased nearly sixfold.

Ontario's Canadian-owned breweries are for the most part synonymous with craft breweries. This report uses these terms interchangeably. While Ontario's craft brewers are diverse, they have some similarities. Their annual production does not exceed 400,000 HL (1 HL = 100 litres), they are not owned by a company whose annual production exceeds 400,000 HL and their philosophies value quality, innovation, and community.

This is the second in a series of Trillium Network for Advanced Manufacturing reports that examine the evolution of Ontario manufacturing between 2010 and 2019. The purpose of these reports is to assess the evolution of the largest (i.e. automotive, see Sweeney, 2020) and fastest-growing (i.e. breweries) manufacturing segments. Information is drawn from government statistics, stakeholder consultations, and other publicly-available sources of data.

The report finds that despite exceptional growth, Ontario's craft brewing industry faces challenges ahead. Some of these are related to the COVID-19 pandemic while others relate to rapid growth and the legislative and policy environment.

Ontario Craft Brewing, 1984-2009

In the early 1980s, a small number of large breweries accounted for virtually all of Ontario's beer production. Following the emergence of craft brewing industries in the US and Britain and facilitated by liberalized brewery and brewpub licensing practices, Ontario craft brewing experienced a boom between the mid-1980s and early 1990s. Several breweries founded during this period continue to operate under independent ownership, including Wellington Brewery, Amsterdam Brewery and Great Lakes Brewery. Several others, such as Creemore Springs, Upper Canada Brewing and Lakeport were acquired by larger breweries between 1998 and 2007. Many more failed outright. Those familiar with the industry say difficulty accessing retail channels and an excise tax system that favoured large producers hindered craft breweries' ability to operate profitably during this era.

The 1990s brought other new entrants. The relatively high cost of beer in Ontario led to a boom in homebrewing and licensed 'brew-your-own' facilities. In fact, several prominent Ontario craft breweries were founded as homebrewing suppliers and 'brew-your-own' facilities. This segment of the industry is often credited with introducing Ontario consumers and producers to styles and flavours that were largely absent from the Canadian market. The 1990s also saw the emergence of a market for discount beer. During this period, several craft brewers pivoted toward servicing this segment and were eventually acquired by larger breweries.

The market for craft beer increased throughout the late 1990s and 2000s. In response, and having learned from the challenges craft brewers faced in the 1980s and 1990s, the governments introduced lower excise taxes and tax credits to encourage growth. These changes recognized that smaller breweries are less likely to achieve the same economies of scale as larger breweries. While the recession of 2008-09 stalled economic growth generally, these changes helped spur growth between 2010 and 2019.

Image Credit - Great Lakes Brewery

A Decade of Growth: Ontario's Craft Brewing Industry, 2010-2019

Between 2010 and 2019, the number of Ontario breweries increased from less than 100 to more than 320. According to the Trillium Network for Advanced Manufacturing's database of Ontario manufacturers, 288 breweries were established in this period. This includes both new companies and new breweries opened by companies that outgrew older facilities. (Amsterdam, for example, moved from downtown Toronto to its Leaside facility in 2012). Fewer than 40 of the breweries currently operating in Ontario were in operation prior to 2010 (Figure 1).

Over the same time the number of persons employed in Ontario craft breweries increased nearly sixfold (Figure 2). Ontario craft breweries employed approximately 800 people (about 35 per cent of Ontario brewery employees) in 2010. This increased to more than 4,600 (nearly 80 per cent of Ontario brewery employees) by 2019. Measured proportionally, the craft brewing industry was the fastest-growing segment of Ontario manufacturing in the decade.

Ontario's craft brewing industry is diverse. Three measures are notable: production capacity, employment, and revenue. The production capacity of Ontario's largest craft brewers is dwarfed by that of internationally-owned brewers in the province. At the same time, the production capacity of the largest craft breweries may be more than 30 times that of smaller breweries. Similarly, several Ontario craft breweries employ more than 100 people across a range of professional and technical occupations. More than 150, however, employ fewer than 10 people (including many that are owner-operated and have no employees). Figure 3 illustrates Ontario craft breweries according to the number of persons employed in 2015 and 2019.[1] While it shows growth across all categories, it identifies an emerging group of approximately 20 breweries with 50 or more employees in addition to the smaller operators. Those 20 account for a substantial proportion of craft brewing employment and output.

Figure 1 – Year Currently Operating Canadian-Owned Breweries were Established

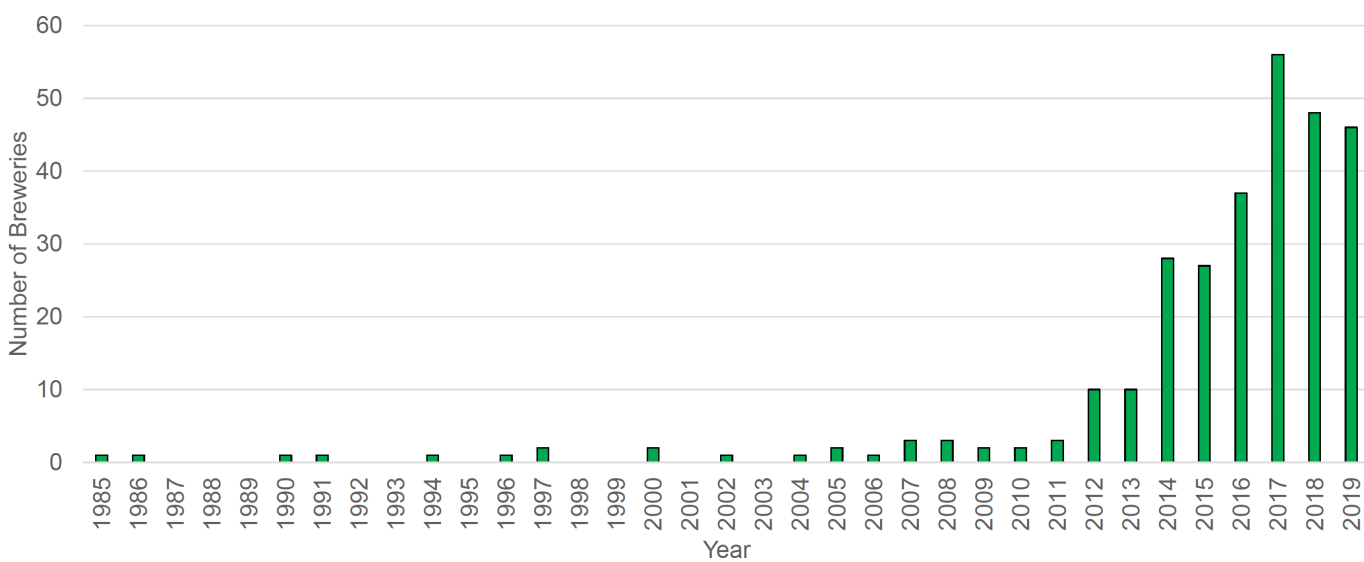
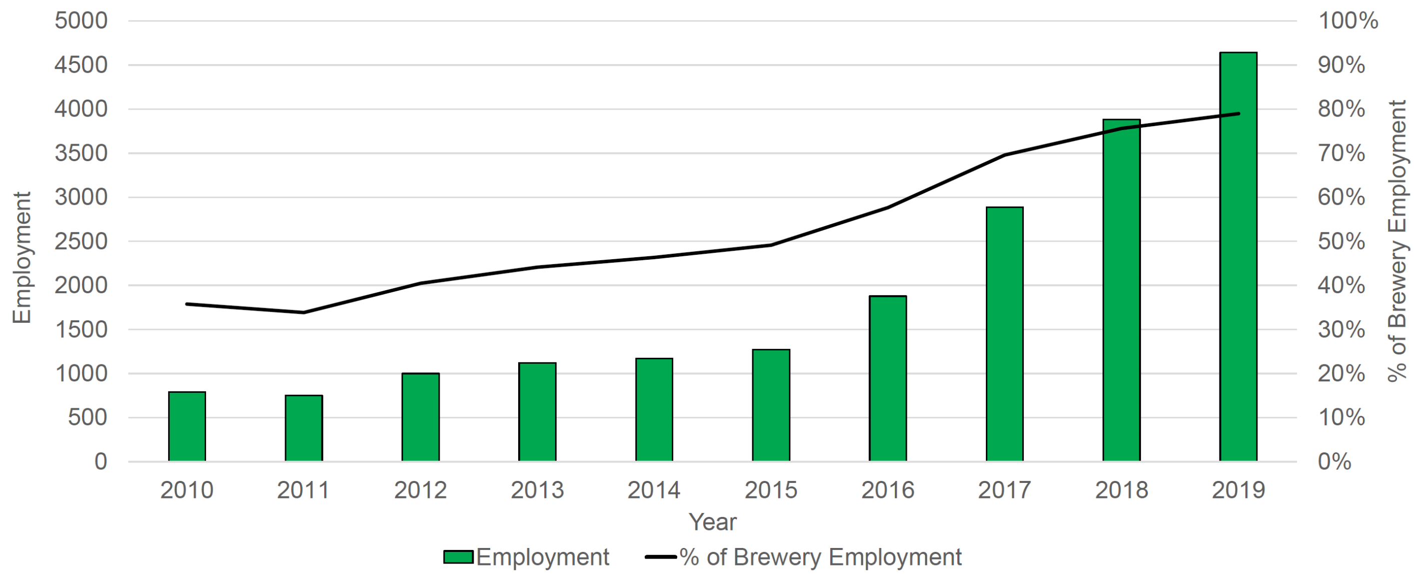
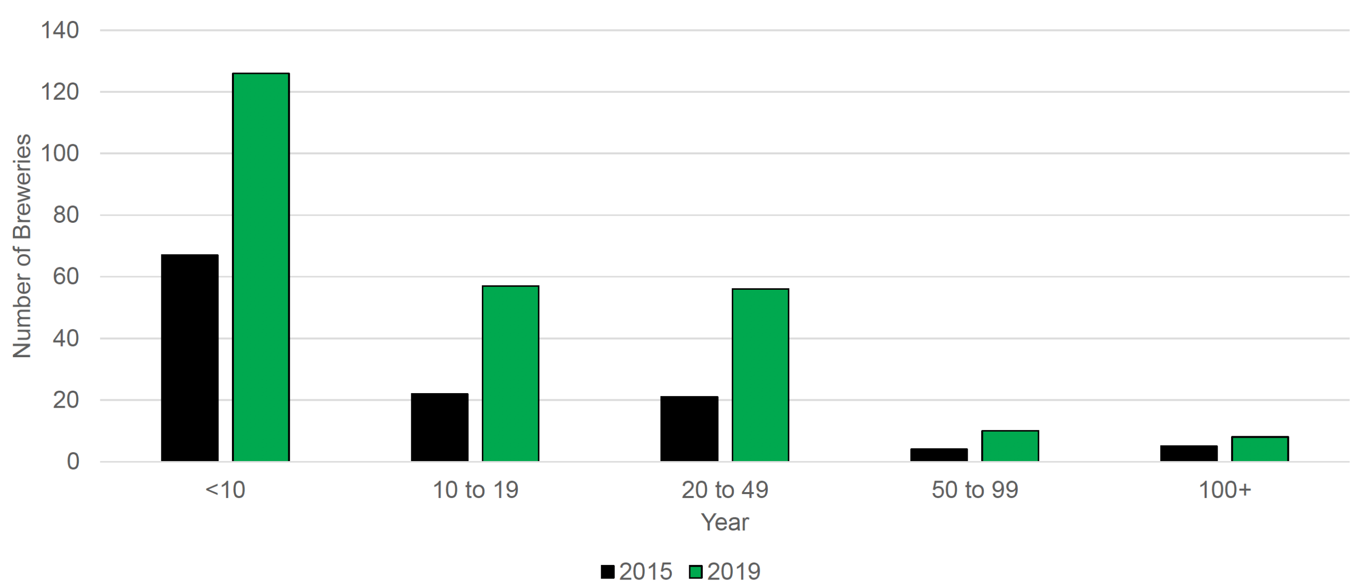


Figure 2 – Canadian-Owned Brewery Employment in Ontario, 2010-2019



■ Data Source: Author's Calculations, Statistics Canada, 2020 (Tables 16-10-0117-01; 16-10-0038-01; 33-10-0222-01); Environment Canada, Various Years.

Figure 3 – Canadian-Owned Breweries by Number of Employees, 2015 and 2019



■ Data Source: Author's Calculations, Statistics Canada, 2020 (Tables 33-10-0039-01; 33-10-0222-01)

Ontario's craft breweries have diverse revenue streams as they operate at a unique intersection of manufacturing, agri-food, tourism, retail and hospitality.

Ontario's craft breweries have diverse revenue streams as they operate at a unique intersection of manufacturing, agri-food, tourism, retail and hospitality. While brewing provides the foundation, the channels through which they sell beer differ, as does the proportion of revenue that each brewery earns from related activities. This distinguishes craft brewers from internationally-owned breweries and many other segments of Ontario manufacturing.

Over the course of this project we identified 11 distinct revenue streams: 1) Taproom Sales, 2) On-Site Retail, 3) Off-Site Retail, 4) Home Delivery, 5) Licensed Establishments, 6) Exports, 7) On-Site Food and Beverage, 8) Events, 9) Merchandise, 10) Other Alcoholic Beverages, and 11) Contract Brewing and Co-Packing. Additional detail is available below. Moreover, several breweries produced sanitizer during the COVID-19 pandemic. We laud their efforts, but have no evidence this will remain part of the industry moving forward.

1. Taproom Sales. Licensed craft breweries sell single servings of their own beer (or multiple small servings, i.e. 'flights') on-site for the purposes of promotion and tourism.

2. On-Site Retail. Craft breweries sell their own beer through on-site retail stores. These stores are often integrated with taprooms. They may only sell beer made by that brewery.

3. Off-Site Retail. Craft breweries sell beer through one of three retail distribution channels: the Liquor Control Board of Ontario (LCBO), The Beer Store (the majority of which is controlled by three internationally-owned brewers and governed provincially), and licensed grocery stores (the majority of which are owned by Loblaws or Sobeys).

4. Home Delivery. Craft breweries increased their home delivery sales substantially during the pandemic. Many may consider home delivery a permanent sales channel.

5. Licensed Establishments. Craft breweries supply restaurants, bars and other alcohol-serving establishments (e.g. arenas, golf courses) with kegs, bottles, or cans.

6. Exports. Some craft breweries export, primarily to such contiguous states as New York or Minnesota. Export opportunities exist, but accessing competitive US markets is challenging.

7. On-Site Food and Beverage. Craft breweries may sell food and other beverages on-site, ranging from snacks to full restaurant service. Some may not serve food directly but invite caterers or food trucks to operate on premises. A full-service restaurant may seem a logical and complementary revenue stream. However, it requires additional licensing, equipment and employees and may place a brewery in direct competition with licensed establishments that it supplies.

8. Events. Many craft breweries offer event space and host weddings, corporate retreats, trivia nights and concerts. Some offer event space free of charge to community groups. Perhaps the most prominent example is Steam Whistle's downtown Toronto brewery, which is among Ontario's most sought after event spaces.

9. Merchandise. Some craft brewers noted that up to 10 per cent of their revenue came from merchandise sales (often shirts and hats).

10. Other Alcoholic Beverage Sales. Several craft breweries have diversified their product offerings by distilling spirits (this requires a separate license). Others apply their brewing expertise to produce (nominally alcoholic) kombucha.

11. Contract Brewing and Co-Packing. Contract brewing (brewing beer for another brewery) and co-packing (packaging someone else's product) are common practices. Craft brewers' opinions on these practices are mixed. More on this below.

What to do About Contract Brewing?

Co-packing models, which involve a third party (usually a specialized packaging company or another brewery) bottling or canning beer for a brewery, are common and do not appear to be a serious concern for industry stakeholders. In fact, mobile canning companies are often heralded for providing innovative solutions to many brewery's challenges related to a lack of space or investment capital. The practice of contract brewing, however, elicits strong opinions from industry stakeholders.

Contract manufacturing is common across the food, beverage, pharmaceutical, and even automotive industries (for example, Canadian automotive parts manufacturer Multimatic assembles the Ford GT supercar on contract at its Markham plant). The brewing industry is no different. Contract brewing occurs when a brewery is contracted to produce beer for a third party. That third party may be a 'bricks-and-mortar' brewery whose production capacity is limited, a 'brewery-in-planning' seeking to bring a product to market while they establish their bricks-and-mortar brewery (often a two-year process), or a 'virtual' brewer without a bricks-and-mortar brewery and with no plans to establish one. The primary advantage of contract brewing is that one can bring a product to market with little to no capital investment. The primary disadvantage is the lack of control over process, quality, or continuity.

The first two practices invite far less controversy than 'virtual' brewing. Several Ontario craft brewers have gone on record outside of this project to decry virtual brewing. Such critics characterize virtual brewing as a short-cut that bypasses the investments craft brewers have made in their production facilities, in accessing retail markets, and in building a community of practice (see Johnson, 2017). Others, however, actively seek opportunities to brew on contract. They perceive these opportunities as good business practice and a means to improve capacity utilization. Amid this controversy, several Ontario breweries that opened in the past five years brew exclusively on contract and have a limited role in marketing and distribution. Up to 90 virtual brewers are active within the province. Despite the controversy surrounding virtual brewing, it is likely to persist as a component of Ontario's brewing industry for the foreseeable future absent legislative changes.[2]

Policy, Legislation, and Governance

A constellation of policies and legislation govern the production, distribution, and sale of beer in Ontario. Many of these policies helped support investments in capital and human resources and provided the foundation upon which Ontario's craft brewing industry was built. Others, particularly those related to market access, present persistent challenges to profitability and further investment and growth.

Changes to provincial taxation laws in 2007 are often seen as the watershed moment that spurred the growth of craft brewing in Ontario. Ontario's tax system generally distinguishes between brewpubs (full-service restaurants or bars that brew beer primarily for on-site consumption) and three types of breweries:

1. Microbreweries, whose annual worldwide beer sales do not exceed 49,000 HL;

2. Small Beer Manufacturers, whose annual worldwide beer sales are between 49,000 HL and 200,000 HL; and

3. Beer Manufacturers, whose annual worldwide beer sales exceed 300,000 HL.[3]

Most of Ontario's craft breweries sell less than 49,000 HL annually and are categorized as microbreweries. As such, their product is subject to excise taxes that are approximately half that of Small Beer Manufacturers and Beer Manufacturers. Microbreweries' excise taxes have, however, increased at a faster proportional rate than those imposed on beer manufacturers over the past decade. This presents challenges for new entrants and those that do not plan to expand their operations.[4]

While higher excise taxes are imposed on Small Beer Manufacturers, they receive a provincial corporate tax credit. The value of this tax credit diminishes as their production exceeds 75,000 HL and is phased out at 200,000 HL. This tax credit is noted to have been particularly helpful for breweries that scaled up production over the past decade. Several craft brewers that participated in this project suggested this tax credit and the reduced excise taxes represented the difference between a profit and a loss in some years.

Dozens of Ontario craft breweries used government incentive programs to support capital investments between 2010 and 2019. These include programs targeted at manufacturers, such as the province's Southwestern Ontario Development Fund (SWODF) and Eastern Ontario Development Fund (EODF), as well as the Federal Economic Development Initiative for Northern Ontario (FedNor). They also include programs targeted at the agri-food sector, such as the provincial-federal 'Growing Forward' programs. Some even benefited from Scientific Research and Experimental Development (SRED) tax credits that supported investments that helped them reduce their environmental footprint.

Public investments in education and research played a role in the industry's growth over the past decade. Praise for the Teaching Brewery and Brewmaster and Brewery Operations program at Niagara College is almost universal among Ontario's craft brewers. This program, which was founded around the same time that the industry's growth trajectory began, provides a base of talent for the industry. The only concern voiced by industry stakeholders was that the program is becoming so well-recognized that Ontario breweries must now compete with those in New York and the US Midwest for Niagara College graduates. The recently-established Durham College Centre for Craft Brewing Innovation has also emerged as an important component of Ontario's craft brewing ecosystem. It provides valuable training, testing and developmental resources and counts a growing number of Ontario craft brewers as partners.

The most significant policy challenges facing Ontario craft brewers are related to market access. Ontario's retail channels are controlled primarily by the LCBO (a provincial Crown corporation), The Beer Store, Loblaws and Sobeys. Our analysis suggests that the challenges that Ontario's craft brewers face in accessing retail markets are best characterized as systemic misalignment.

The LCBO's annual revenue exceeds $6 billion. The Beer Store's annual revenue exceeds $400 million and it is controlled by three companies whose combined annual revenue is more than $60 billion. Loblaws' annual revenue is about $48 billion and Sobeys' is more than $25 billion. The sophisticated retailing, marketing, and distribution practices of these organizations may be well-aligned with those of well-capitalized internationally-owned brewers and services a large segment of the market. Yet these retailing practices appear to be misaligned with craft breweries and inhibits their attempts to satisfy demand for their product. Ontario's craft brewers are growing rapidly despite limited market access. This raises a key question: would that growth be stronger if market access were improved?

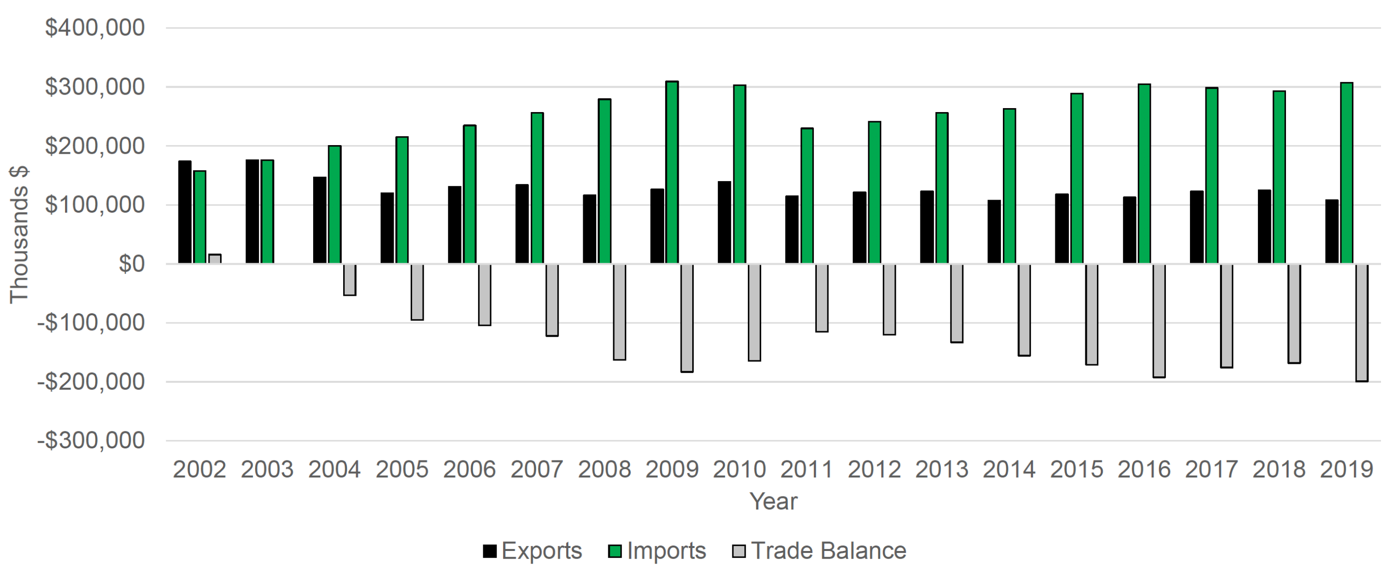
Trade policy also affects Ontario craft brewers. Several export to the United States and others aspire to do so. While opportunities exist, exporting to notoriously competitive US markets comes with its own challenges. A potentially more germane issue are increases in international beer imports to Ontario.

Ontario had a surplus in the trade of beer as recently as the early 2000s. This has since shifted to a substantial deficit (Figure 4). This deficit is related primarily to increased imports from the EU.

Improving consumer access to Ontario-made beer may prove a useful means to reduce the province's dependence on imports from the EU

Improving consumer access to Ontario-made beer may prove a useful means to reduce the province's dependence on imports from the EU amid uncertainty surrounding international trade. It is also likely to have positive impacts on employment and economic contributions, which may prove critical to post-pandemic recovery efforts.

Figure 4 – Ontario Brewery Trade Balance, 2002-2019



Data Source: ISED Canada Trade Data Online, 2020

What's Next for Ontario's Craft Brewing Industry?

Ontario's craft brewing industry grew substantially over the past decade. A fascinating group of craft brewers and partners including the Ontario Craft Brewers (OCB), the Canadian Craft Brewers Association, Niagara College, and Durham College emerged alongside, creating a community that values collaboration and innovation. The growth of Ontario's craft brewing industry was the result of a combination of entrepreneurial spirit, policy supports and consumer demand. At the same time, the industry faces a number of challenges. Some are directly related to the COVID-19 pandemic and are shared across the economy. Others are more specific to craft brewing. Similarly, our analysis has identified several additional areas of future inquiry.

Small Policy Changes have Significant Impacts. Ontario's craft brewing industry is sensitive to policy and legislative changes. Seemingly small changes to taxation can mean the difference between profit and loss for a craft brewer in any given year. Investment incentives tend to expedite capital upgrades and lead to increased output and employment. Exploring innovative opportunities to improve craft brewers' access to markets – perhaps using wine retailing as a model – may foster further growth and increased economic contributions.

Employment: Quantity and Quality? The report identifies the growth in the number of persons employed in Ontario's craft brewing industry between 2010 and 2019. Less is known, however, about other aspects of employment, such as the distribution of employees across occupations, employee demographics, earnings, and career trajectories within the industry. A better understanding of employment opportunities and career paths may be a useful area of inquiry.

Capital Intensive Craft Brewing? It is understandably difficult for smaller craft breweries to achieve the same levels of capital intensity as larger breweries. That said, some have made significant investments in modern production technologies, including digitization. Whether this will provide these breweries with a competitive edge (as is common elsewhere in Ontario manufacturing, see Boothe et al., 2019) and whether these types of technologies will be more widely adopted by craft brewers is another potentially valuable area of inquiry.

Room to Grow? Ontario's craft brewing industry grew substantially over the past decade. The entry rate was extremely high, while the rate of exits or closings, was exceptionally low. This raises important questions about whether the industry can maintain this trajectory. It also raises questions about the structure of the industry, especially if growth plateaus. There is some recent evidence of consolidation through mergers and acquisitions, but more analysis over a longer period is necessary to draw informed conclusions. Questions about capacity utilization have also emerged as the industry grows.

COVID-19. The economic impacts of the COVID-19 pandemic will be significant. While Ontario's craft brewers have developed strategies to mitigate some of the damage to their businesses, such as home delivery of beer and production of hand sanitizers, the impacts on taproom sales, events and other tourism-based activities will be severe. Survey data collected by the OCB suggest that more than 50 per cent of craft brewery employees have been temporarily displaced during the pandemic. Understanding these impacts may prove useful in developing supports to put the craft brewing industry back on its previous trajectory of growth as Ontario emerges from the pandemic. Questions regarding the elasticity of demand for premium products may also emerge if economic challenges persist.

References

Boothe, P., A. Smith, and D. Zhang. 2019. Catching the Wave: Lessons from Ontario's Digital Manufacturing Early Adopters. Trillium Network for Advanced Manufacturing.

Available here:
https://trilliummfg.ca/wp-content/uploads/2020/04/e.-Publications-Catching-The-Wave.pdf

Johnson, B. 2017. 'Contract' Brewing Boom in Ontario Stokes Debate over Future of Craft Beer. *The Globe and Mail*, 6 July 2017.

Sweeney, B. 2020. Canada's Automotive Industry: A Decade in Review. Trillium Network for Advanced Manufacturing.

Available here:
https://trilliummfg.ca/wp-content/uploads/2020/05/TrilliumReport_AutoIndustry-DecadeInReview-May2020_2A.pdf

[1] These data do not include owner-operated bricks-and-mortar breweries without employees.

[2] All the breweries that participated in this project were Canadian-owned with bricks-and-mortar facilities. None of the exclusively contract-brewing companies nor 'virtual' breweries participated, despite invitations by the author.

[3] Two of Ontario's Canadian-owned breweries fall into this category. The Waterloo Brewing Company and Hop City Brewery, which is a subsidiary of the New Brunswick-based Moosehead Breweries.

[4] The federal government also collects specific excise taxes tiered according to production, although these taxes are far less than those collected by the province.

TRILLIUM NETWORK
FOR ADVANCED MANUFACTURING

Trillium Network for Advanced Manufacturing
Room 6306
Social Science Centre
Western University
London, ON N6A 5C2

info@trilliummfg.ca

519 661 3351