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REDHOOK BREWING COMPANY

Craft Brewing Goes Public

In August 1995, Paul Shipman, the CEO of Red Hook (RH) prepared himself to enter uncharted territory. A craft brewing operation had never before been taken public in the United States, and he and his management team were about to do just that. Sure, there were massive large-batch breweries like Anheuser-Busch and Miller Brewing Company that were profitable, publicly traded firms—but there was something different about Red Hook: it embodied the ethos and grassroots beginnings of the microbrew movement, and Shipman was confident that widespread market demand for craft beer was set to explode.

He and the team had steadily developed their premium-quality handmade ales for nearly fifteen years, and their loyal customer base was strong. In the last year alone, he'd forged alliances with both Starbucks (for the purposes of co-branding a coffee-flavored brew) and A-B that had purchased a capped 25% interest in RH in exchange for access to its national distribution networks and accounting systems. Shipman had overseen significant capacity increases, with plans on the horizon for yet another brewery in Portsmouth, New Hampshire. He had worked hard to position RH favorably for expansion, and the public offering would provide the necessary capital. But how would the "microbrew" feel of RH translate to the large-scale commercialization and growth pressures of the open market? Producing and distributing microbrews on a large scale was a new concept—and like any new concept, it would have to be sold. Shipman hoped to sell craft beer—and lots of it—in the heartland of America.

Revolutionary Beginnings

Shipman thought back through the determined, tumultuous beginnings of the company he had helped to found after graduating from the Darden School of Business at the University of Virginia in 1980. RH was brought to life in 1981 in Seattle, Washington by Shipman and his friend Gordon Bowker, who had previously founded and run Starbucks for twelve years and who wanted try his hand at beer. Their first investor was Bowker's acquaintance Jerry Jones, who

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contributed $30K in exchange for a seat on the board of directors as vice president.[1] Redhook Ale Brewery was thus founded—but they did not yet own a brewery or even have a recipe. One of their first actions was to hire Charles McElevey, an award-winning Seattle brewmaster, to develop the first Redhook ales.

Shipman estimated that they needed $350 thousand in order to build their first brewery and stay afloat in the meantime. He approached a number of wealthy Seattle contacts with a detailed prospectus that included the following:

> Redhook Ale will be produced to fill a specific position in the marketplace which, in the opinion of management, is not presently occupied by an existing product: that of a freshly brewed, locally produced beverage that is competitive in both taste and price with the best-selling imported beers and ales.
>
> The increasing sales of import beers are testimony to the existence of enthusiastic and experimental beer drinkers. A recent profile based on research by *Business Week Magazine* reveals that import beer drinkers tend to be young (25 to 44 years), affluent, and managerial persons.[2]

The prospectus detailed a number of risks—including the potential loss of McElevey, upon whom they were dependent to make their product. Shipman and Bowker, after exhausting their entire list of prospective investors, succeeded in selling $175K in common stock, half of their goal—but a sufficient minimum capitalization to build their brewery and stay in business.[3]

Bowker and Shipman continued to conduct fundraising activities in an attempt to attract additional investors, ultimately reaching the $350 thousand target. They also bought and cleaned up an old transmission shop in Seattle, and McElevey painstakingly reconstructed a recycled brewery that he located and had shipped from Germany. Many test batches and recipes later, the trio were happy with their first product and planned a grand opening on August 11, 1982—which was attended by both the mayor of Seattle and the governor of Washington State.[4] Their marketing strategy was primarily word-of-mouth; they began their marketing campaign by reaching out to local restaurants, bars and brewpubs to carry kegs of their beer, which was delivered in early years by a single truck.[5]

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[1] Krebs, Peter. *Redhook: Beer Pioneer*. Four Walls Eight Windows: New York, 1998. p 52.
[2] Krebs, 60.
[3] Krebs, 68.
[4] Krebs, 80.
[5] Krebs, 87.

Development of a Distinctive Beverage

RH beer was brewed by a special system that involved adding fresh hops to freshly milled grain, fermenting with proprietary yeast in a temperature-controlled vat and employing a filtration process. The bottled beer was not exposed to the air until it was opened by the consumer—and was hand-dated for peak consumption within 14 days. RH's attention to the highest quality, traditional European brewing methods and locally sourced ingredients helped them to build a strong local reputation and loyal consumer following.

> Shipman wanted to control every aspect of the process, from the equipment used, the processes employed, to the people who brewed the beer. Shipman once compared brewing a beer such as Redhook ESB to the making of a house specialty in a fine restaurant: each time, every aspect of the preparation had to be near perfect. It wasn't enough to have fresh ingredients and follow the recipe. The equipment used had to be top quality to ensure precision, and the staff had to be carefully trained in order to execute the same dish flawlessly time and time again. Only by building their own breweries and training their own staff, Shipman believed, could Redhook achieve the level of quality he was after.[6]

While RH's distinctive offering was the consistent, premium quality of its product, its primary growing pains lay in managing the relationship between its sales growth projections and increased capacity needs—and balancing this against the need to maintain and grow a strong brand presence. At first, RH sold directly to restaurants, pubs and retailers in the Seattle area using mostly a word-of-mouth advertising strategy. It was truly a craft-beer-darling startup story, complete with humble beginnings in a renovated old trolley shop and quality-obsessed management team. They even found a sculptor to design custom ceramic taps when they became large enough to distribute kegs in local restaurants.

Growth and Expansion

They grew quickly throughout the mid-to-late 1980s at rates sometimes exceeding 25% a month. In 1985, Shipman and Bowker wanted to move beyond selling kegs to restaurants, and worked to open a bottled line. They had some difficulty for many months as they attempted to establish bottling processes that captured the freshness and flavor to which Redhook's customers had grown accustomed. During this time, they also lost their full-time brewmaster, but successfully worked with their 13 employees to increase their compensation packages and ward off a looming union threat.[7]

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[6] Krebs, 2.
[7] Krebs, 150-153.

Through a series of calculated capacity expansions in the Northeast region, RH had managed the sales growth-versus-capital investment tradeoff, with a capacity of 250,000 barrels in reach. Shipman knew that the increased capacity he and his team had planned for represented yet another major shift, this time from local Seattle darling to nationally recognized brand. See Exhibit 1 for RH's capacity growth and future estimates.

Since 1981, RH had engaged in several rounds of financing, including the initial round that raised $350,000 and two subsequent rounds that tripled their capitalization. In 1994, his arrangement with Anheuser-Busch had resulted in the issuing of Series B preferred stock to Anheuser that gave the mass brewer a 25% stake in RH. At that time, an extraordinary $2 dividend per share was paid to existing shareholders with the proceeds of the sale. Shipman contemplated what should be done with the proceeds of the pending IPO. He had several ideas but was unsure which he and his team would ultimately choose. For instance, RH could further compensate the company's first investors for their early support, virtually eliminate the firm's debt, commit the funds to the business in the form of capacity or technology development, or invest capital on building the RH brand on a national scale.

The Craft Beer Phenomenon

Trends in Beer

Craft beer had been around since humans had been fermenting grain and grapes—but grassroots microbrewing had been limited, post-prohibition, to fringe garage-and-basement operations. From 1934 through the mid 1980s, most U.S. beer consumption was either first- or second-tier national brands or imports, which were primarily from Europe. Available retail beer offerings became increasingly homogeneous as the large U.S. brewers consolidated their positions and achieved economies of scale. By some standards, this was achieved in part by reducing quality—including product pasteurization, using ingredients that were not as fresh as they could be and generally shortcutting the process of making quality beer. The first-tier brands were Anheuser Busch, Miller Brewing Company and Coors and the second tier consisted of around ten smaller competitors such as Stroh, Heileman, Pabst and Genesee. See Exhibit 2 for a breakdown of all barrels shipped by first and second-tier brewers, as well as "All Others" and imported beer, 1990-1994.

From 1975 to 1995, U.S. beer consumption per capita varied only slightly, rising from the 17-19 gallons per year range, peaking in the early 80s around the 24-gallon mark and then steadily declining, settling in the range of 22-23 gallons per year. Industry volume has shown essentially zero growth since the early 1980s; between 1984 and 1994 the U.S. beer industry shipped product at the relatively flat rate of around 180,000 barrels per year.[8] This lack of industry growth, combined with weakening performance in the second-tier group may have been

[8] M.J. Rietbrock et. al, "Redhook Ale Brewery," Analyst Report, Smith Barney, September 15, 1995, p. 13.

what allowed the major players to consolidate their position relative to the runners-up. The deteriorating robustness of the second-tier brewing category might have been attributable to their less-competitive economies of scale and lower margins—which in a fixed or declining market would result in the decreased ability to sufficiently reinvest in capital equipment and the promotion of new brands. The second-tier brewers began to lose their relevancy during this ten-year span. (See Exhibit 3.)

Beginning around 1984, craft beer began to take hold as a primarily regional phenomenon. These beers were typically priced higher than their mass-produced counterparts and were more comparable in terms of price point to the super-premium mass-produced beverages or European imports. As U.S. craft brewers built a locally supported presence in the American landscape—given the fact that the market itself was not expanding—the impact of consumer substitution was primarily felt by European imports. *Fortune* wrote in 1995: "While total domestic beer sales slumped 0.6% in 1994, craft brews grew by 44%. The industry should grow more than 50% this year [1995.] That will give [craft brewers] perhaps 2% of the market. But industry watchers see the segment grabbing a 7% to 10% market share by 2000.[9]

Demographics

Craft brew drinkers tended to be highly educated and have high incomes—the largest income bracket of craft beer consumers by far was the over-$75,000 tier—but these divisions were widening over time as a broader cross-section of people were becoming introduced to the product. A 1994 national survey of beer drinkers, with a focus on microbrew drinking habits—the first of its kind—indicated that the greatest concentration of exposure was in the 20- to 30-something range, with 36% of adults 25-34 years old having tried a microbrew, compared with 27% of adults aged 35-44 and only 20% of adults over 45. Men were more likely than women to have tried one, and people of Caucasian descent were twice as likely to have tried one than individuals of African-American descent. Geography, too, played a role. The most pronounced regional preference was revealed in the West, with 32% of beer drinkers reporting that they had tried a microbrew, compared to 29% in the Northeast, 25% in the Midwest and only 18% in the South. Interestingly, consumption and exposure data from New York, Los Angeles and Chicago revealed low market penetration in each of these, the three most populous metropolitan areas. [10]

Shipman knew that part of Redhook's success was similar to that of Starbucks coffee: the craft beer value proposition was not just about finely crafted beer; in addition, craft beer was also about selling a particular identity through repetition consumable product. Drinking craft beer said something about the consumer. It said: "I support local business," and "I care about quality," and, ultimately, "I am unique too." This reality was echoed in the affinity scores earned by top-

[9] Gunn, Eileen. *Microbrew Party On Wall Street.* Fortune, Section: Newstrends. 12/11/95, Vol. 132 Issue 12, p28-30, page 28.

[10] Student, John. American Demographics, May 95, Vol. 17 Issue 5, p32.

tier beer manufacturers in a 1995 study conducted by the impartial BBDO New York ad agency. Affinity scores are determined by showing photographs of a variety of people to a random sample of test subjects and asking them which beer each photographed individual is likely to drink. Then, test subjects are asked whether he or she relates well to (or has affinity for) the person in the photograph. The scores were revealing of prevailing New-York-based attitudes towards mass produced beers:

> Budweiser scored 42% -- not good, since this means that most respondents didn't view the Bud man as likable. Coors's affinity score, 43%, is hardly better. Says Karen Olshan, BBDO New York's executive vice president in charge of research: "The Coors drinker was perceived as not a real beer drinker." The most positive user image belongs to Miller. Its affinity score is 66%.[11]

In contrast, craft beers invoked their microbrew roots to entice consumers to buy an emblem of authenticity, uniqueness, and local cache. Even their labels and packaging were often designed to invoke a localized, contrarian aesthetic intended to appeal to a younger, increasingly affluent generation of customers.

Craft Beer, Unpacked

The craft brew segment was made up of small regional specialty brewers (1,000,000-15,000 barrels per year) and microbrews (less than 15,000 barrels per year.) Brewpubs, which were restaurants that produced and sold in-house brands of beer, were sometimes considered part of this segment but were thought of by some analysts to be essentially a restaurant concept. These three sub-segments owned and operated their own equipment, which was capital intensive and involved close attention to building and maintaining production capacity relative to current and projected production needs—in addition to brand development and sales responsibilities. A fourth segment, the contract brewer, outsourced brewing to other brewers but provided a recipe and brew specifications. The benefit to this model was that capacity utilization was theoretically always at 100%, and it was sometimes possible to take advantage of the contract brewers' economies of scale for sourcing ingredients.

The largest regional specialty brewer in terms of total taxable revenues was Sierra Nevada Brewing Co., followed by Anchor Brewing Co. and then Redhook. Hart Brewing Company, makers of Pyramid ales and Thomas Kemper lagers, was fourth, just after Redhook (See Exhibit 4). Hart had shipped 33,000 barrels of Pyramid ales and 7,000 barrels of Thomas Kemper lagers in 1993 and, when they came up against the limitations of their current in-house brewing capacity, had a different growth strategy than did RH. The five Hart owners knew that neither contract brewing, outside investment dollars nor an alliance with a mass producer was for them. In 1995, they were also not looking at an IPO as a desirable option. Their marketing was

[11] Sellers, Patricia. *Fortune*, 9/19/94, Vol. 130 Issue 6, p83.

limited to direct consumer product sampling and feedback—and they stayed away from large campaigns. The owners said, in a July 1995 interview:

> If we were to deal with a major brewery, it would have to be a 100% deal…plenty of those conversations have taken place, [but] we're not in discussions right now…our strategy is a little different from most. Ours is to be a local supplier of fresh-brewed product…we think the whole appeal is diversity, the fact that you can't get it somewhere else. If all specialties become available everywhere, they are no longer so special.[12]

A fourth important craft brewer category was the contract brewing company—the largest of which was Boston Beer (BB), makers of the popular Sam Adams brand. These companies had entirely different capital needs because their brewing was contracted out to a third party, which usually took the form of a second-tier brewer looking to fill idle capacity. Contract brewers came up with a "recipe" and brewing specifications, outsourced the actual brewing and bottling (which other craft brewers did not do, often as a point of pride) and then developed brands and managed sales and distribution. Contract brew production rose from only 9,000 barrels in 1985 to over 1 million in 1994—while regional specialty brew production rose from around 38,000 barrels to just over 730,000 during that same time span, with an average CAGR of 61% and 34%, respectively. Brewpubs represented about 10% of the craft beer business, growing from around 1,400 barrels in 1985 to over 260,000 in 1994 with a CAGR of 68%, and microbrews rose from around 25,000 barrels to over 450,000 with a CAGR of 33%.[13] See Exhibit 5 for differences in operational spending between BB and RH.

Such comparisons highlight the key differences in business models between the two key competitors, and more broadly, the difference between contract and in-house brewing and their implications for scaling up craft brewing operations. Redhook's position was that contract sourcing violated the entire point of craft brewing, and essentially represented consumer deception. In addition, Shipman was publicly skeptical of the stability of the contract brewer business model itself, and felt that Redhook's approach offered a contrast to "mirco marketers who rely on contract brewers." Observing that the pricing stability, availability, and consistent quality of contract capacity was dependent largely on forces outside of Boston Beer's control, Shipman suggested that:

> "Retailers ought to know there could be terrible interruptions" in the production pipeline if the contractors do indeed go out of business. "When breweries go under, they begin to look like the engine room of the Titanic. It's not pretty."

As to suggestions by the likes of Boston Beer president Jim Koch that his

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[12] Kelley, Kristine Portno. *A strong Hart.* Beverage Industry, Jul95, Vol. 86 Issue 7, p29-32. Section: Corporate Focus.

[13] Rietbrock, 26.

> company should really be called "Budhook," Shipman shoots back that Koch's contract-brewed Samuel Adams ought to be known as "Scam Adams."
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> "I did not pick this fight," Shipman insists, "but I am not going to walk away from this. Consumers should be revolted that contract brewers misrepresent themselves."[14]

Exhibit 5 shows an estimated margin analysis of RH and BB. Between 1991 and 1994, they each grew rapidly, leading their respective sub-segments in the growing craft beer market. BB was well positioned in 1994 with nearly 8 times the sales volume of RH, but with a much higher advertising cost and lower margins. BB's marketing and advertising cost was almost 50% of sales—while RH's marketing was primarily word-of-mouth and represented only about 20% of sales. RH's operating margins had historically fluctuated between 20 and 25% in comparison to the 4-7% range of BB.

Big Beer, Interrupted

In 1994, possibly due to the flat-to-slowly-declining category volume, demographic changes and zippy growth in the craft beer segment, first-tier beer manufacturers began to flirt with strategies designed to capture some of this emerging specialty brew market. This took many forms. Some purchased stakes in or formed partnerships with existing craft beer manufacturers. After Anheuser-Busch and RH disclosed their distribution deal, reports circulated that Miller and Seagram, a non-alcoholic beverage company, were doing the same.[15] Others developed a more varied, upscale product line intended to appeal to that same demographic. Some of these new products were intended to be perceived by the less-educated buyer as unique and craft brew in nature; others, like the "ice" beers, were simply an attempt at novelty and variety:

> Last year, the giants of America's beer industry started thinking small. Anheuser-Busch, the largest brewer in the U.S., bought a stake in Seattle's Redhook Ale Brewery. Coors Brewing Company scored with Killian's Irish Red, which sounds like a Dublin pub brew but is actually pumped out of a huge factory in Colorado. And the advertising for another successful new product, Ice-house, featured the down-home employees of the Plank Road Brewery. Read the fine print on the bottle, and you'll discover that Plank Road is actually produced by the Miller Brewing Company.[16]

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[14] Prince, Greg W. *Though he's hooked up with the biggest one, Shipman says he'll still brew independently. (Paul Shipman, chairman of Red Hook Ale Brewery Inc.)* Beverage World Periscope Edition, 30 June 1995, Vol. 114, No. 1594, ISSN: 1064-8909, p. 18.

[15] Sellers, p. 82

[16] Student, p. 32-33

> Says Anheuser-Busch CEO August Busch III, 57: "I don't think there's going to be a completely new way to make beer or a breakthrough as there was in the Seventies with light beer." But this year the industry has introduced about 40 -- count 'em -- new "ice" beers. Pure gimmickry? You bet. Ice beers, first developed in Canada, are beers produced at temperatures just a few degrees colder than ordinary brew, which gives them a slightly above-average alcohol content. Still, "ice" has turned out to be one cool marketing ploy. The products have captured almost 6% of industry sales -- more than all imports combined.[17]

In mid-1995, to say that the industry was changing was an understatement. Shipman wondered: Could the craft brew segment, in particular the regional specialty brewer as compared to the contract brewer, sustain its recent high growth? Would one model win out over the other as industry dynamics continued to surprise? There were other players to consider, too, now that RH would be going national. The first- and second-tier players had been caught off-guard by craft beer and were scrambling to claim their piece of the microbrew pie.

Pre-IPO Musings

Shipman knew that he had significant growth projections to live up to after his company went public. He felt that $17 per share was a fair offering price, and he hoped that RH would gain an advantage by being first to tap the craft brew public share market. The scarcity of being first on the scene might create even more demand.

His company was in great shape: their brewing technology was first-rate, mostly brand new and running well. His capital structure was strong, cash flow high, and long-term debt manageable (See Exhibit 6 for RH’s financials). He felt that the combined experience of his management team only built more public confidence in the RH success story. Their product was still premium—bottles were still individually date-stamped and the fresh, hops-forward brew continued to be sealed from contact with the air until opened by the consumer.

There were other factors that Shipman knew would have an effect on RH’s performance over the next several years:

> The Company's capacity utilization has a significant impact on gross profits. When facilities are operating at their maximum designed production capacity, profitability is favorably affected by spreading fixed and semivariable operating costs, such as depreciation and production salaries, over a larger sales base. Most capital costs associated with building a new brewery and fixed and semivariable costs related to operating a new brewery are incurred prior to, or upon commencement of, production at a facility. Because the initial production level is

[17] Sellers, p. 79

> substantially below the facility's maximum designed production capacity, gross margins are negatively impacted. This impact is reduced as the facility's actual production increases. In addition, as the Company's total production capacity increases, the impact on gross margins of each additional facility will be reduced. In addition to capacity utilization, the Company expects other factors to influence profit margins, including higher costs associated with the opening of new distribution territories, such as increased shipping, marketing and sales personnel costs; fees related to the distribution agreement with Anheuser-Busch, Inc. ("A-B"); changes in packaging and other material costs; and changes in product sales mix. The incremental cost of shipping beer from the Company's breweries will continue to increase as the volume of beer supplied to more distant markets increases. The Company believes that full-scale production at the Portsmouth Brewery will reduce shipping expenses to eastern U.S. markets. Also, the Company's ability to connect directly to the City of Portsmouth water line is subject to approval of design plans and weather conditions. There is no assurance as to the timing of such direct connection, although the Company anticipates completing the connection in the second quarter of 1997. Until the direct connection is complete, the cost of tankering water from the City of Portsmouth's system, or other sources, for production purposes at the Portsmouth Brewery will negatively impact gross profit.[18]

In addition to operating risks, Shipman understood that RH's future primarily depended on the acceptance of a premium product in geographic areas that had not before been regularly exposed to craft beer as a higher-priced alcoholic beverage option. In fact, the behavioral demographics of craft beer drinkers in general were still up for debate. After all, Shipman had to sell his *vision* internally and to his shareholders, and he had to sell his *reliability* to suppliers and distributors—but he had to sell his *product* to consumers—and therefore much depended upon whether he would be able to pull off in New Hampshire and Tennessee what he had accomplished in the Pacific Northwest. Shipman had continued to promote the RH niche-market brand through interviews that adamantly sent the message that their play for national distribution was merely a response intended to meet popular demand from their customers. One article read:

> What was available initially in the west had been catching on elsewhere even before the A-B alliance took effect. For example, Shipman found a ready-made market in Wichita, KS. The reason: Wichita, like Seattle, is a hub of aircraft manufacturing, and personnel who relocated from Washington to Kansas spread the Redhook word.

[18] 1995 Company 10-k, retrieved from SEC January 3, 2012.

> "We began to get very heavy inquiries around '91, '92 from retailers and distributors," says Shipman. "Our reputation pulled us into the rest of the country."[19]

Shipman also needed to remain focused on his primary competitor: Boston Beer. They would be going public soon, too—as might Pete's Wicked Ale, Hart and any number of other craft beer firms. Certainly, BB would continue to pose a threat to RH, since the Boston firm enjoyed greater economies of scale than did RH, and currently dominated the Northeast craft brew market. But Shipman remained convinced that contract brewers like BB and Pete's couldn't be sure about the quality or consistency of their products. Those businesses had to grapple with the availability of the idle capacity they needed to keep their own utilization at 100%, forcing them to rely upon distressed second-tier brewers to do their manufacturing for them. And BB spending 50% of gross sales in marketing and advertising? RH had never had to do that. Sam Adams was a good craft beer, but RH was a purer manifestation of the microbrew ethic. But confidence did not equate to strategy; the compelling question involved how RH should compete with BB going forward. And beyond competing with BB, how could RH seize customers away from the mass brewers? More broadly, how much growth potential existed in the craft brewing industry segment?

And of course the immediate matter at hand was the public offering. As RH prepared to go public, the question most raised by analysts was: What is the value of RH's equity? How would the first day of trading turn out? Was the implied growth rate of RH sustainable? How would the first tier mass brewers react to RH's capitalization?

[19] Prince, p.18

Exhibit 1

REDHOOK BREWING COMPANY

Capacity Growth in Barrels per Year

1982	Ballard Brewery	30,000
1989	Freemont Brewery phase 1	40,000
1993	Freemont Brewery phase 2	Additional 35,000 (total 75,000)
Sept. 1994	Woodinville Brewery phase 1	60,000
July 1995	Woodinville Brewery phase 2	Additional 110,000 (total 170,000)

Estimated Growth in Barrels per Year

Late 1996	Woodinville Brewery phase 3	Additional 80,000 (total 250,000)
Late 1996	Portsmouth, NH Brewery phase 1	100,000
Late 1997	Portsmouth, NH Brewery phase 2	Additional 150,000 (total 250,000)
1999	Midwest brewery	300,000
Total estimated capacity by 1999:		875,000

Source: M.J. Rietbrock et. al, “Redhook Ale Brewery,” Analyst Report, Smith Barney, September 15, 1995, p.6.

Exhibit 2

REDHOOK BREWING COMPANY

Brewer's Shipments, 1990 – 1994 (in 000s)

	1990	1991	1992	1993	1994
Anheuser-Busch	86,499	86,037	86,846	87,306	88,159
Miller	43,500	43,556	42,145	44,024	45,200
Coors	19,300	19,550	20,000	20,000	20,200
Stroh	16,200	14,800	14,000	12,610	11,850
Heileman	10,914	9,377	9,133	8,940	8,315
Pabst	6,700	6,600	6,900	7,000	6,630
Genesee	2,200	2,220	2,150	2,000	1,800
Latrobe	713	803	882	1,035	1,060
Falstaff/Pearl/Genesee	850	800	900	800	700
Pittsburgh	700	700	670	575	470
Top Brewers	187,576	184,443	183,626	184,290	184,384
All Others	2,591	3,514	5,097	5,492	6,818
Domestic Brewers	190,167	187,957	188,723	189,782	191,202
Imports	8,922	8,031	8,409	9,348	10,602
Total	199,089	195,988	197,132	199,130	201,804

Notes: Anheuser-Busch figure for 1994 excludes 370,000 bbls of Kirin Ice contract-brewed for Kirin.
Miller figure for 1994 includes 2.3M bbls of Molson products; Miller 1993 includes 1.2M bbls of Molson.
Coors figures adjusted to show shipments for calendar years.
Pittsburgh numbers do not include contract brewing performed for Boston Beer (Sam Adams).
"All Others" includes approximately 425,000 bbls of malt beverages used in malt coolers.

Source: M.J. Rietbrock et. al, "Redhook Ale Brewery," Analyst Report, Smith Barney, September 15, 1995, p. 14.

Exhibit 3

REDHOOK BREWING COMPANY

Market share of top-tier, second-tier and “other” brewers, 1985 and 1994

	1994	1984
A-B	44.2%	34.5%
Miller	22.7%	20.2%
Coors	10.1%	7.0%
"2nd Tier"	13.4%	28.1%
All Others	9.6%	10.2%

Source: M.J. Rietbrock et. al, “Redhook Ale Brewery,” Analyst Report, Smith Barney, September 15, 1995, p. 14.

Exhibit 4

REDHOOK BREWING COMPANY

Regional Specialty Brewers, 1993 and 1994

	1994	1993	% Change
Sierra Nevada Brewing Co	155,942	104,325	49.5%
Anchor Brewing Co.	102,462	92,000	11.4%
Redhook Ale Brewery	93,577	73,000	28.2%
Pyramid Ales / Hart Brewing Co (includes Thomas Kemper Brewing Co)	72,416	39,200	84.7%
Full Sail Brewing Co.	52,598	38,159	37.8%
Widmer Brewing Co.	50,000	40,520	23.4%
Portland Brewing Co.	36,994	16,606	122.8%
Stevens Point Brewing Co.	31,000	N/A	N/A
Straub Brewery	27,000	N/A	N/A
Rockies Brewing Co.	26,180	17,900	46.3%

Source: M.J. Rietbrock et. al, "Redhook Ale Brewery," Analyst Report, Smith Barney, September 15, 1995, p. 19.

Exhibit 5

REDHOOK BREWING COMPANY

Financial Summary, Red Hook and Boston Beer, 1991 – 1994

	Red Hook				Boston Beer			
	1991	1992	1993	1994	1991	1992	1993	1994
Percentage Margin Analysis								
Net Sales	100%	100%	100%	100%	100%	100%	100%	100%
COGS	57.4	55.3	53.7	58.2	44.3	45.7	46	46
Gross Profit	42.6	44.7	46.3	41.8	55.7	54.3	54	54
SG&A	21.5	19.9	17.4	18.8	48.7	50.6	47.7	46.2
Operating Income	21.1	24.8	28.9	23.1	7	3.7	6.3	7.7
Other Income	-2.1	-2.4	-1	-0.8	0.1	-0.3	0	0.2
Pre-Tax Income	19	22.4	27.9	22.2	7.1	3.4	6.3	7.9
Net Income	12.5	15.6	18.3	14.2	4.2	2	3.7	4.6
Per Barrel Analysis								
Net Sales	$170.50	$164.02	$156.03	$159.50	$169.29	$163.87	$162.42	$160.83
COGS	$97.91	$90.65	$83.74	$92.80	$74.94	$74.93	$74.70	$74.02
Gross Profit	$72.59	$73.37	$72.30	$66.70	$94.36	$88.95	$87.73	$86.81
SG&A	$36.65	$32.62	$27.18	$29.93	$82.48	$82.93	$77.46	$74.36
Operating Income	$35.94	$40.75	$45.12	$36.77	$11.87	$6.02	$10.27	$12.45
Other Income	($3.50)	($3.98)	($1.60)	($1.30)	$0.13	($0.42)	$0.00	$0.28
Pre-Tax Income	$32.44	$36.77	$43.52	$35.48	$12.01	$5.60	$10.26	$12.72
Net Income	$21.29	$25.56	$28.59	$22.70	$7.07	$3.24	$6.01	$7.45

	Red Hook				Boston Beer			
	1991	1992	1993	1994	1991	1992	1993	1994
<u>Financial Returns</u>								
EBIDTA to Total Capital	NA	28.10%	21.40%	13.50%	NA	19.40%	16.80%	72.60%
Net Income to Common Equity	26.70%	25.40%	31.50%	167.40%	20.70%	14.80%	32.20%	80.60%

Source: M.J. Rietbrock et. al, "Redhook Ale Brewery," Analyst Report, Smith Barney, September 15, 1995, p. 26.

Exhibit 6

REDHOOK BREWING COMPANY

Excerpts from Redhook's Offering Prospectus

11

As filed with the Securities and Exchange Commission on August 15, 1995
Registration No. 33-94166

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

RECD S.E.C.
AUG 15 1995
FEE 033

AMENDMENT NO. 2
TO
Form S-1/A
REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

EXECUTED COPY

95 18 1045

REDHOOK ALE BREWERY, INCORPORATED

(Exact name of registrant as specified in its charter)

Washington	**2082**	**91-1141254**
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

3400 Phinney Avenue North
Seattle, Washington 98103
(206) 548-8000
(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

PROCESSED BY
83 — 79 — I
AUG 16 1995

Bradley A. Berg
Executive Vice President and Chief Financial Officer
3400 Phinney Avenue North
Seattle, Washington 98103
(206) 548-8000
(Name, address, including zip code, and telephone number, including area code, of agent for service)

DISCLOSURE INCORPORATED
L10

Copies to:

John M. Steel, Esq. Riddell, Williams, Bullitt & Walkinshaw 1001 Fourth Avenue Plaza, Suite 4400 Seattle, Washington 98154 (206) 624-3600	Stephen A. McKeon, Esq. Perkins Coie 1201 Third Avenue, 40th Floor Seattle, Washington 98101-3099 (206) 583-8888

Approximate date of commencement of proposed sale to the public:
As soon as possible after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box: ☐

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act of 1933, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering: ☐ ________

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act of 1933, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering: ☐ ________

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box: ☐

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to Be Registered	Amount to Be Registered(1)	Proposed Maximum Offering Price Per Share(2)	Proposed Maximum Aggregate Offering Price(2)	Amount of Registration Fee
Common Stock, par value $0.005 per share	2,250,106 shares	$17.00	$38,251,802	$13,190

(1) Includes 293,492 shares that may be purchased by the Underwriters from the Registrant to cover over-allotments, if any.

(2) Estimated solely for the purpose of computing the registration fee pursuant to Rule 457(a) under the Securities Act of 1993, of which $11,638 has previously been paid.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

TOTAL OF SEQUENTIALLY NUMBERED PAGES 83
EXHIBIT INDEX ON SEQUENTIALLY NUMBERED PAGE 80

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Exhibit 6 (continued)

The Offering

Common Stock Offered Hereby by:	
The Company	1,900,000 shares
The Selling Shareholders	56,614 shares
Common Stock Offered in the Concurrent Placement(1)	618,883 shares
Common Stock and Preferred Stock Outstanding After the Offering and the Concurrent Placement(2)	8,582,045 shares
Use of Proceeds	For repayment of borrowings, construction of the Portsmouth Brewery, and general corporate purposes. See "Use of Proceeds."
Nasdaq National Market Symbol	HOOK

(1) Assumes no change in the number of outstanding shares of capital stock between the date hereof and the date of the Concurrent Placement. Does not include an additional 97,831 shares issuable to A-B pursuant to its preemptive right if the Underwriters' over-allotment option is exercised in full.

(2) Includes 1,289,872 shares of Series B Preferred Stock, which are convertible into the same number of shares of Common Stock, and reflects the conversion of all 1,242,857 shares of the Company's convertible Series A preferred stock (the "Series A Preferred Stock") into the same number of shares of Common Stock upon consummation of the Offering. Does not include 417,042 shares of Common Stock issuable at a weighted average exercise price of $10.23 per share upon exercise of stock options outstanding as of July 31, 1995. See "Description of Capital Stock — Preferred Stock," "Management — Benefit Plans — Stock Options" and Notes 5 and 6 of Notes to Annual Financial Statements.

USE OF PROCEEDS

The net proceeds to the Company from the sale of the 1,900,000 shares of Common Stock being offered by the Company hereby, assuming an initial public offering price of $15.00 per share, after deducting estimated Underwriting Discounts and Commissions and estimated expenses of the Offering payable by the Company, and from the Concurrent Placement of 618,883 shares offered by the Company at the assumed initial public offering price, are estimated to be approximately $35.3 million ($40.8 million if the Underwriters' over-allotment option is exercised in full). The Company intends to use a portion of the estimated net proceeds to repay borrowings incurred in connection with the final phase of construction at the Woodinville Brewery and project costs relating to the Portsmouth Brewery. At June 30, 1995, such borrowings totaled approximately $9.1 million and were accruing interest at 7.3% per annum. Such borrowings are currently payable in June 1997. The Company will use the remaining net proceeds for the completion of the final phase of the Woodinville Brewery, for construction of the Portsmouth Brewery, and for general corporate purposes. In addition, a portion of the net proceeds may be used for the acquisition of complementary product lines or businesses. Although there are currently no negotiations, commitments, or agreements with respect to any such acquisitions, the Company will consider acquisition opportunities as they arise. Pending the above uses, the net proceeds will be invested in short-term, liquid investments.

The Company will not receive any proceeds from the sale of Common Stock by the Selling Shareholders.

Exhibit 6 (continued)

SELECTED FINANCIAL DATA

The following selected financial data should be read in conjunction with the Company's Financial Statements and the Notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Prospectus. The selected income and balance sheet data for, and as of the end of, each of the four years in the period ended December 31, 1994, are derived from the financial statements of the Company, which were audited by Ernst & Young LLP, independent auditors. The selected income and balance sheet data for, and as of the end of, the year ended December 31, 1990, and each of the six-month periods ended June 30, 1994 and 1995, are derived from the unaudited financial statements of the Company. The operating data are derived from unaudited information maintained by the Company. Management believes that the unaudited financial statements include all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation of the Company's financial position and results of operations. Operating results for the six months ended June 30, 1995, are not necessarily indicative of the results that may be expected for any other interim period or for the year ending December 31, 1995.

	Year Ended December 31,					Six Months Ended June 30,	
	1990	1991	1992	1993	1994	1994	1995
	(In thousands, except per share and operating data)						
Statement of Income Data:							
Sales	$ 4,302	$ 6,156	$ 8,593	$12,331	$16,209	$ 6,734	$12,284
Less Excise Taxes	258	359	507	847	1,280	559	1,111
Net Sales	4,044	5,797	8,086	11,484	14,929	6,175	11,173
Cost of Sales	2,443	3,329	4,469	6,162	8,686	3,304	7,354
Gross Profit	1,601	2,468	3,617	5,322	6,243	2,871	3,819
Selling, General and Administrative Expenses	921	1,246	1,608	2,001	2,801	1,148	1,974
Operating Income	680	1,222	2,009	3,321	3,442	1,723	1,845
Interest Expense	110	94	236	158	130	—	—
Other Income (Expense), Net	19	(25)	40	40	9	(37)	24
Income Before Income Taxes	589	1,103	1,813	3,203	3,321	1,686	1,869
Provision for Income Taxes	200	379	553	1,099	1,196	607	673
Income Before Accounting Change	389	724	1,260	2,104	2,125	1,079	1,196
Change in Accounting for Taxes	—	—	—	99	—	—	—
Net Income	$ 389	$ 724	$ 1,260	$ 2,005	$ 2,125	$ 1,079	$ 1,196
Per Share:							
Income Before Accounting Change	$ 0.12	$ 0.23	$ 0.39	$ 0.51	$ 0.41	$ 0.22	$ 0.19
Net Income(1)	$ 0.12	$ 0.23	$ 0.39	$ 0.49	$ 0.41	$ 0.22	$ 0.19
Dividends per Share(2)	—	—	—	—	$ 2.00	—	—
Average Number of Common and Equivalent Shares Outstanding	3,184	3,184	3,258	4,134	5,156	4,914	6,173
Operating Data (in barrels):							
Barrels Shipped	23,600	34,000	49,500	73,900	93,700	40,900	68,900
Production Capacity, End of Period(3)	30,000	40,000	60,000	75,000	135,000	37,500	87,500

	December 31,					June 30, 1995
	1990	1991	1992	1993	1994	
	(In thousands)					
Balance Sheet Data (End of Period):						
Working Capital (Deficit)	$ (150)	$ 1,055	$ (566)	$ 1,735	$ (842)	$ (464)
Total Assets	3,853	7,382	9,949	20,044	34,689	43,924
Long-term Debt, Net of Current Portion	892	2,923	3,014	2,066	3,793	10,955
Series A Preferred Stock	—	—	—	8,335	8,956	9,258
Series B Preferred Stock	—	—	—	—	15,834	15,856
Common Stockholders' Equity	1,989	2,713	4,952	6,683	1,269	2,152

(1) A portion of the net proceeds from the Offering will be used to repay certain indebtedness. If, at the beginning of the year ended December 31, 1994 and the six-month period ended June 30, 1995, the Company had sold a sufficient number of shares at $15.00 per share to repay the indebtedness, and used the net proceeds therefor, pro forma net income per share would have been $0.40 and $0.17 for the respective periods.

(2) Consists entirely of a one-time extraordinary dividend paid to shareholders other than A-B from the proceeds of the sale of Series B Preferred Stock to A-B.

(3) Based on the Company's estimate of production capacity of equipment installed as of the end of such period, assuming, among other things, production five days per week, two shifts per day. At times, production may exceed the Company's estimate of production capacity. Production Capacity (End of Period) for the year ended December 31, 1994 and the six months ended June 30, 1995 does not reflect maximum designed production capacity. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Overview."

Exhibit 6 (continued)

BALANCE SHEETS

ASSETS

	December 31, 1993	December 31, 1994
Current Assets:		
Cash and Cash Equivalents	$ 2,456,119	$ 472,487
Accounts Receivable	930,581	1,146,218
Inventories	260,925	578,430
Federal Income Tax Receivable	125,674	326,361
Prepaid Expenses and Other	36,522	70,208
Total Current Assets	3,809,821	2,593,704
Other	108,156	657,312
Fixed Assets, Net	16,126,100	31,437,539
Total Assets	$20,044,077	$34,688,555

LIABILITIES, REDEEMABLE PREFERRED STOCK AND COMMON STOCKHOLDERS' EQUITY

	1993	1994
Current Liabilities:		
Accounts Payable	$ 1,325,762	$ 2,097,412
Accrued Salaries, Wages, and Payroll Taxes	231,290	454,665
Refundable Deposits	332,432	515,705
Other Accrued Expenses	72,432	248,029
Current Portion of Long-term Debt	113,139	120,014
Total Current Liabilities	2,075,055	3,435,825
Long-term Debt, Net of Current Portion	2,065,862	3,793,421
Deferred Income Taxes	859,129	1,380,897
Other	25,808	19,514
Commitments and Contingencies		
Convertible Redeemable Preferred Stock, Series A and B	8,335,269	24,789,928
Common Stockholders' Equity:		
Common Stock, Par Value $0.005 Per Share — Authorized, 20,000,000 Shares; Issued and Outstanding, 3,068,320 Shares in 1993 and 3,529,576 Shares in 1994	15,342	17,649
Additional Paid-In Capital	2,302,822	1,112,539
Retained Earnings	4,364,790	138,782
Total Common Stockholders' Equity	6,682,954	1,268,970
Total Liabilities, Redeemable Preferred Stock and Common Stockholders' Equity	$20,044,077	$34,688,555

Exhibit 6 (continued)

REDHOOK ALE BREWERY, INCORPORATED

STATEMENTS OF INCOME

	Year Ended December 31,		
	1992	1993	1994
Sales	$8,593,128	$12,331,081	$16,209,072
Less Excise Taxes	507,223	846,918	1,279,976
Net Sales	8,085,905	11,484,163	14,929,096
Cost of Sales	4,469,203	6,162,979	8,685,653
Gross Profit	3,616,702	5,321,184	6,243,443
Selling, General and Administrative Expenses	1,607,650	2,000,595	2,801,465
Operating Income	2,009,052	3,320,589	3,441,978
Interest Expense	236,395	158,184	130,105
Other Income, Net	40,041	40,398	8,647
Income Before Income Taxes	1,812,698	3,202,803	3,320,520
Provision for Income Taxes	552,761	1,098,636	1,195,606
Income Before Cumulative Effect of Accounting Change	1,259,937	2,104,167	2,124,914
Cumulative Effect of Change in Accounting for Income Taxes	—	98,714	—
Net Income	1,259,937	2,005,453	2,124,914
Preferred Stock Accretion	—	274,412	632,284
Income Applicable to Common Stock	$1,259,937	$ 1,731,041	$ 1,492,630
Per Share:			
Income Before Accounting Change	$0.39	$0.51	$0.41
Net Income	$0.39	$0.49	$0.41

Exhibit 6 (continued)

REDHOOK ALE BREWERY, INCORPORATED

STATEMENTS OF COMMON STOCKHOLDERS' EQUITY

	Common Stock				
	Shares	Par Value	Additional Paid-In Capital	Retained Earnings	Total Common Stockholders' Equity
Balance, January 1, 1992	2,768,320	$13,842	$1,324,952	$1,373,812	$2,712,606
Sale of Common Stock	300,000	1,500	977,870	—	979,370
Net Income	—	—	—	1,259,937	1,259,937
Balance, December 31, 1992	3,068,320	15,342	2,302,822	2,633,749	4,951,913
Preferred Stock Accretion	—	—	—	(274,412)	(274,412)
Net Income	—	—	—	2,005,453	2,005,453
Balance, December 31, 1993	3,068,320	15,342	2,302,822	4,364,790	6,682,954
Sale of Common Stock	236,756	1,184	1,656,144	—	1,657,328
Stock Options Exercised	224,500	1,123	575,803	—	576,926
Income Tax Benefit From Exercise of Stock Options	—	—	263,486	—	263,486
Note Receivable for Stock Purchase	—	—	(333,000)	—	(333,000)
Preferred Stock Accretion	—	—	—	(632,284)	(632,284)
Dividends	—	—	(3,352,716)	(5,718,638)	(9,071,354)
Net Income	—	—	—	2,124,914	2,124,914
Balance, December 31, 1994	3,529,576	$17,649	$1,112,539	$ 138,782	$1,268,970

Exhibit 6 (continued)

REDHOOK ALE BREWERY, INCORPORATED

STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	1992	1993	1994
Operating Activities			
Net Income	$1,259,937	$2,005,453	$ 2,124,914
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Depreciation and Amortization	370,071	529,046	762,455
Cumulative Effect of Accounting Change	—	98,714	—
Deferred Income Tax Provision	221,686	377,290	521,768
Other	(21,982)	(607)	(6,243)
Changes in Operating Assets and Liabilities:			
Accounts Receivable	(228,307)	(429,040)	(215,637)
Inventories	17,084	7,780	(317,504)
Income Tax Receivable	(297,870)	(10,400)	(200,687)
Prepaid Assets and Other	(14,745)	(14,958)	(108,232)
Accounts Payable and Other Accrued Expenses	36,366	(158,987)	947,247
Accrued Salaries, Wages and Payroll Taxes	35,252	66,591	223,375
Refundable Deposits	70,450	134,732	183,273
Net Cash Provided by Operating Activities	1,447,942	2,605,614	3,914,729
Investing Activities			
Expenditures for Fixed Assets	(4,628,432)	(6,154,350)	(14,576,956)
Deposits on Equipment	—	(780,453)	(1,857,176)
Proceeds From Sales and Other	105,090	21,931	(11,873)
Net Cash Used in Investing Activities	(4,523,342)	(6,912,872)	(16,446,005)
Financing Activities			
Proceeds From Short-term and Long-term Debt	475,000	874,000	12,645,747
Repayments on Short-term and Long-term Debt	(322,353)	(2,193,171)	(10,911,365)
Proceeds From Sale of Preferred Stock	—	8,060,857	15,822,375
Proceeds From Sale of Common Stock	979,370	—	1,657,328
Exercise of Stock Options, Including Tax Benefit	—	—	507,412
Dividends Paid	—	—	(9,071,354)
Other	—	(71,761)	(102,499)
Net Cash Provided by Financing Activities	1,132,017	6,669,925	10,547,644
Increase (Decrease) in Cash and Cash Equivalents	(1,943,383)	2,362,667	(1,983,632)
Cash and Cash Equivalents:			
Beginning of Year	2,036,835	93,452	2,456,119
End of Year	$ 93,452	$2,456,119	$ 472,487