CRAFT BREW ALLIANCE, INC.
Form 10-K
March 14, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549
FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Fiscal Year Ended: December 31, 2011
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File Number: 0-26542

CRAFT BREW ALLIANCE, INC.
(Exact name of registrant as specified in its charter)

Washington (State or other jurisdiction of incorporation or organization)	91-1141254 (I.R.S. Employer Identification No.)
929 North Russell Street Portland, Oregon (Address of principal executive offices)	97227-1733 (Zip Code)

Registrant's telephone number, including area code: (503) 331-7270

Securities Registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $0.005 par value	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes o No x

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K, or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. Large accelerated filer o Accelerated filer x Non-accelerated filer o (Do not check if a smaller reporting company) Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No x

The aggregate market value of the common equity held by non-affiliates of the registrant as of the last day of the registrant's most recently completed second quarter on June 30, 2011 (based upon the closing price of the registrant's common stock, as reported by the NASDAQ Stock Market, of $8.61 per share) was $89,701,391.

The number of shares outstanding of the registrant's common stock as of March 5, 2012 was 18,844,817 shares.

Documents Incorporated by Reference

Portions of the registrant's definitive Proxy Statement for the 2012 Annual Shareholders' Meeting are incorporated by reference into Part III.

CRAFT BREW ALLIANCE, INC.
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INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This annual report on Form 10-K includes forward-looking statements. Generally, the words "believe," "expect," "intend," "estimate," "anticipate," "project," "will," "may," "plan" and similar expressions or their negatives identify forward-loo statements, which generally are not historical in nature. These statements are based upon assumptions and projections that we believe are reasonable, but are by their nature inherently uncertain. Many possible events or factors could affect our future financial results and performance, and could cause actual results or performance to differ materially from those expressed, including those risks and uncertainties described in "Item 1A. - Risk Factors" and those described from time to time in our future reports filed with the Securities and Exchange Commission. Caution should be taken not to place undue reliance on these forward-looking statements, which speak only as of the date of this annual report.

THIRD-PARTY INFORMATION

In this report, we rely on and refer to information regarding industry data obtained from market research, publicly available information, industry publications, U.S. government sources or other third parties. Although we attempt to utilize third-party sources of information that we believe to be materially complete, accurate and reliable, there is no assurance of the accuracy, completeness or reliability of third-party information.

PART I

Item 1. Business

Overview

Craft Brew Alliance (formerly known as Craft Brewers Alliance) is the union of three unique pioneering craft breweries:

- Redhook Ale Brewery founded by Gordon Bowker and Paul Shipman in 1981 in Seattle, Washington;
- Widmer Brothers Brewing founded by brothers Kurt and Rob Widmer in 1984 in Portland, Oregon; and
- Kona Brewing Co. founded by father and son team Cameron Healy and Spoon Khalsa in 1994 in Kona, Hawaii.

Since our formation, we have focused our business activities on satisfying consumers through the brewing, marketing and selling of high-quality craft beers in the United States. Today, as an independent craft brewer, we possess several distinct and ownable advantages unique in the craft beer category. These advantages are rooted and leveraged through the combination of our innovative portfolio of distinct, authentic brands; national sales and marketing reach with seamless national distribution; bi-coastal breweries with significant available capacity; and five brew pubs supporting consumer awareness and research and development.

We operate in two segments: Beer Related operations and Pubs and Other. Beer Related operations include the brewing and sale of craft beers from our five breweries. Pubs and Other operations primarily include our five pubs, four of which are located adjacent to our breweries.

We proudly brew our Widmer Brothers, Redhook and Kona beers in each of our three company-owned mainland production breweries that are located in Portsmouth, New Hampshire ("New Hampshire Brewery"); Portland, Oregon (the "Oregon Brewery"), which is our largest brewery; and in the Seattle suburb of Woodinville, Washington ("Washington Brewery"). Our brewery located in Kailua-Kona, Hawaii ("Hawaiian Brewery") brews our Kona branded beers. We also own and operate a small manual style brewery, primarily used for small batch production and innovative brews, at the Rose Quarter in Portland, Oregon.

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In all 50 states, we are wholly aligned with the distributors who are part of the Anheuser-Busch, LLC ("A-B") distribution network. We sell our beers primarily to these wholesalers via a Master Distributor Agreement ("A-B Distributor Agreement") with A-B. Redhook and Widmer Brothers beers are distributed in all 50 states and Kona beers are distributed in 29 states. Separate from our A-B wholesalers, we maintain an independent sales and marketing organization complete with resources across the key functions of brand management, field marketing, field sales, and national retail sales.

Acquisition of Kona Brewery, LLC ("Kona")

As a result of the closing of the merger with Kona Brewing Co., Inc. (the "KBC Merger") on October 1, 2010, Kona became a wholly-owned subsidiary and, accordingly, Kona's results of operations are included in our consolidated results of operations from that date. Prior to the KBC Merger, we accounted for our 20% equity ownership interest in Kona under the equity method of accounting. We acquired Kona Brewing Co., Inc. ("KBC") in exchange for $6.2 million in cash and 1,667,000 shares of our common stock with a value of $11.7 million.

Sale of Equity Interest in Fulton Street Brewery, LLC ("FSB")

On May 2, 2011 we sold our 42% equity interest in FSB to A-B for $16.3 million.

Industry Background

We are a brewer in the craft brewing segment of the U.S. brewing industry. The domestic beer market is comprised of ales and lagers produced by large domestic brewers, international brewers and craft brewers. Shipments of craft beer in the United States are estimated by industry sources to have increased by approximately 14.5% in 2011 over 2010 and by 11.4% for 2010 over 2009. Although the overall domestic market experienced a decrease in 2011, the craft beer segment continued its growth and captured market share from the rest of the domestic market. Craft beer shipments in 2011 and 2010 were approximately 5.5% and 4.9%, respectively, of total beer shipped in the U.S. Approximately 11.3 million barrels and 9.9 million barrels, respectively, were shipped in the United States by the craft beer segment during 2011 and 2010, while total beer sold in the U.S., including imported beer, was 204.9 million barrels and 208.0 million barrels, respectively. Compared with the other segments of the U.S. brewing industry, craft brewing is a relative newcomer. Twenty years ago, Redhook and Widmer Brothers Brewery were among the approximately 200 craft breweries in operation. At the end of 2011, the number of craft breweries in operation had grown to 1,900. Industry sources estimate that craft beer produced by regional and national craft brewers, similar to us, accounts for approximately two-thirds of total craft beer sales, with one-third of the production brewed by smaller craft breweries.

The recent competitive environment has been characterized by two divergent trends; the number and diversity of craft brewers have significantly increased while, simultaneously, the national domestic brewers have acquired or been acquired by other national domestic and foreign brewers. In 2011, according to industry sources, A-B and MillerCoors accounted for more than 85% of total beer shipped in the United States, excluding imports. Certain national domestic brewers have invested in existing smaller craft breweries and created separate craft-focused divisions in an effort to capitalize on the growing craft beer segment.

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Business Strategy

Our consumer mission is to satisfy more consumers, at more times, in more locations through more authentic, distinct craft beer and brands than any other competitor.

The central elements of our business strategy include:

- An innovative portfolio of distinct, authentic craft beer brands. We have brought together a collection of brands from original innovators in the craft beer industry to enable us to match individual brands to a variety of consumer preferences. Through beer taste profiles and brand personalities, customers are able to forge a strong relationship with the targeted brands. The breadth of our product offerings also provides consumers with the opportunity to match specific consumer occasions with a product in our brand families.

- National sales and marketing reach combined with seamless national distribution. We believe that we are able to leverage our national sales and marketing capabilities and complementary brand families to create a unique identity in the distribution channel and with the consumer. We believe that the combination of the complementary brand families promoted by one integrated sales and marketing organization delivers both financial benefits and greater impact at the point of sale. We have invested in technologies that allow us to not only focus our brand families and product offerings on those markets and regions that represent the most significant opportunities, but also measure the results of those efforts. Our sales force has been structured to be able to call on all retail channels nationally, including grocery, drug and convenience stores, where most other craft brewers are not able to do so.

We distribute our products in substantially all of our markets through A-B’s wholesale distribution network. A-B’s domestic network consists of more than 510 independent wholesale distributors, most of which are geographically contiguous, and 14 wholesale distributors owned and operated by A-B. This distribution relationship with A-B has offered efficiencies in logistics and product delivery, state reporting and licensing, billing and collections. We have realized these efficiencies while maintaining full autonomy over the production, sale and marketing of our products as an independent company. Recent developments in the relationship between A-B and its independent wholesalers have led to an increase in craft and specialty brewers with access to this channel.

- Bi-coastal brewing capability with significant additional capacity. Our breweries are located on both coasts and in Hawaii, which allows for efficient brewing and distribution of our beers. Each of our breweries is modern and has flexible production capabilities. Our New Hampshire and Oregon Breweries have room for bolt-on capacity additions. We prefer to own and operate all of our breweries to optimize the quality and consistency of our products and to achieve greater control over our production costs. We may engage third party brewers to provide contract brewing from time to time to further expand our packaging and brand offerings. We believe that maximizing the production under our direct ownership and through selection of accomplished and expert partners is critical to our success. Further, we believe that our ability to engage in ongoing product innovation and to control product quality provides critical competitive advantages. Our highly automated breweries are designed to produce beer in smaller batches relative to the national domestic brewers, thereby allowing us to brew a wide variety of brand offerings. We believe that our investment in brewing and logistic technologies enables us to minimize brewery operating costs and consistently produce innovative beer styles and tastes.

- Five brew-pub restaurants supporting consumer awareness and research and development. Our five brew-pub restaurants allow us to interact directly with over one million consumers annually in our home markets, which creates a sense of brand loyalty. Our brewers are continually experimenting with new and different varieties of hops and malts in all styles of beer. Our brew-pubs provide us with the opportunity to bring those beers to market in test-size batches in order to understand their strengths prior to releasing them on a national level.

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Beers

Our beer portfolio is comprised of the Widmer Brothers, Redhook and Kona brand families.

We produce a variety of specialty craft beers using traditional European brewing methods adapted by American innovation and invention. We brew our beers using high-quality hops, malted barley, wheat, rye and other natural and traditional ingredients. To help maintain full flavor, our products are not pasteurized and we apply a freshness date to our products for the benefit of wholesalers and consumers. We generally distribute our products in glass bottles and kegs.

Within each brand family, we have created several types and styles of craft beer that align with a variety of consumer taste preferences. We have created year-round brands and flagship brands that help define our brand families' identities; these are the brands that consumers usually think of when they think of our brand families, and are usually the most widely available.

Seasonal brand offerings provide the consumer compelling variety on the retail shelf or at the pub, restaurant or bar. Many of these brand offerings are brewed to match the seasonal change in weather, specific events (e.g. Oktoberfest) or popular activities and are replaced with new offerings when the season or conditions change. These brands allow our brewers to experiment and innovate with ingredients and brewing styles. Additionally, each of the brand families has developed a wide range of high-end brands, some of which are offered as limited releases, that are offered exclusively at our restaurants and pubs.

Given the long relationship that many consumers have had with each of the brands and the growing consumer interest in high-end craft beers, we have also developed a select group of higher-end specialty beers that are brewed, bottled and packaged in a manner befitting the unique nature of these beers. Our high-end brands are marketed toward the beer connoisseur, a rapidly emerging class of consumer within the craft beer segment. We have deliberately limited the shipment volumes associated with our high-end beers to retain the rarity and uniqueness of these beers to the connoisseur community.

The brands within each of the brand families are categorized below, with details provided for key year round contributors within each of the families. These brands are usually offered both in draft and packaged formats.

Widmer Brothers Beers
The Widmer Brothers beers are unique interpretations of classic beer styles meant to expand beer drinkers' perceptions of these styles; they frequently use newly developed hop varieties and unusual ingredients in their recipes. Key brands within the Widmer Brothers brand family are:

Widmer Brothers Hefeweizen

- Widmer Brothers Hefeweizen. The top selling beer within the brand family is a golden, cloudy wheat beer with a pronounced citrus aroma and flavor. This beer is intentionally left unfiltered to create its unique appearance and flavor profile and is usually served with a lemon slice to enhance the beer's natural citrus notes. This beer's relatively low alcohol content by volume makes it perfect for consumption as a session beer. Its most recent award, among many, was the 2008 World Beer Cup Gold medal winner for the American-style Hefeweizen category.

Widmer Brothers core beers

- Drifter Pale Ale ("Drifter"). Drifter possesses a unique citrus character, smooth drinkability, and a distinctive hop character. Brewed with generous amounts of Summit hops, a variety known for its intense citrus flavors and aromas, this beer has a taste unique to the Pale Ale category. This beer started as a seasonal offering, becoming a year round brand in 2009, and was a Great American Beer Festival (“GABF”) Silver Medal Winner in 2006 for the American-style Pale Ale category.

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- Drop Top Amber Ale. A 2010 World Beer Cup Gold Medal Winner and a 2008 GABF Gold Medal Winner.
- Rotator India Pale Ale ("IPA"). Rotator IPA is a unique series of beers, offered in limited quantities, which change throughout the year to highlight different hops and styles.

Widmer Brothers high-end beers

- Series 924. Named for the Oregon Brewery's address, the beers in this brand are made for those who share our passion for the art of brewing and the taste for authentic beers. Initial beers in the 924 Series include the Nelson Imperial IPA and the Pitch Black IPA, which is a Pacific Northwest twist on a traditional IPA, brewed in the style of a Cascadian Dark, an emerging style. Beers in this brand are offered as a draft product and as a four pack for bottles. Pitch Black IPA was the 2009 GABF Gold Medal Winner.
- Brothers' Reserve. This brand is the specialty high-end offering for the Widmer Brothers brand, with only two offerings a year. The beers chosen for this brand reflect the passion and uniqueness of the Widmer brothers and are extremely limited. The brand is focused on the knowledgeable and enthusiastic beer lover who is looking for something exclusive, rare and collectible.
- Alchemy Project. Named for the proprietary hop blend that serves as the foundation for many Widmer Brothers beers, the Alchemy Project is a new series of vintage-dated beers that can be enjoyed immediately or cellared for years. Barrel Aged Brrbon '11 was the first release under the Alchemy Project in the fall of 2011.

Widmer Brothers seasonal beers

- Citra Blonde. A very smooth, light, refreshing beer for summer time. Features Citra hops.
- Okto. Full bodied with malty flavor, containing a floral aroma and finish. Available late summer and fall.
- Brrr. A bold, hoppy northwest red ale brewed with a sweet candy finish for the cold winter months.
- W Series. Designed to demonstrate our brewers' creativity, brewing a variety of styles. Available as the Widmer Brothers spring seasonal.

Redhook Beers
The Redhook family of beers is comprised of sessionable (lower alcohol by volume) and approachable beers with character that push style boundaries without being over the top. Key brands within the Redhook family are:

Redhook core beers

- Long Hammer IPA ("Long Hammer"). Long Hammer is the top-selling beer within the brand family and is an English pub-style bitter ale with a bold hop aroma and profile that is not overpoweringly bitter.
- Redhook Pilsner ("Pilsner"). Pilsner is the newest addition to Redhook's core lineup; a crisp, easy-drinking, golden lager that is modeled after historic beers originally brewed in Plzen, Czechoslovakia.

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- Redhook ESB ("ESB"). ESB is modeled after the high-end Extra Special Bitters found in classic English pubs. ESB is a rich, full-bodied amber ale with a smooth flavor profile featuring toasted malts and a pleasant finishing sweetness.

- Copperhook Ale. A brilliant copper-colored ale with distinctive caramel notes and a clean refreshing finish.

- Blueline Series. This brand is the high-end offering from the Redhook brand family for the West Coast beer drinker. These beers are hand crafted by the brewers and are available at our Washington Brewery pub, as well as at select restaurants, bottle shops, and public houses in the Seattle, Washington area.

- Brewery Backyard Series. This brand is produced at our New Hampshire Brewery as a draft product available only at the brewery's pub and at select local establishments. These high-end beers are experimental in nature and designed to appeal to craft beer connoisseurs and the community of self-described beer geeks. Like the Blueline Series, the Brewery Backyard Series is intended to be locally-relevant.

Redhook seasonal beers

- Nut Brown Ale. A medium-bodied, brown ale with a fresh aroma. Available late winter and spring.

- Winterhook Winter Ale. Red chestnut in color and full-bodied with a toasty, complex profile. Available late fall and winter.

- Wit. Redhook's twist on the Belgian style is the addition of fresh ginger, which adds a refreshing snappiness to this lighter-bodied wheat beer. Redhook Wit is available during the summer months.

Kona Beers
The Kona brand family is comprised of beers that deliver the authentic essence of the Hawaiian Islands that is "Always Aloha." The Aloha Series in the Kona brand family uses ingredients that are unique to the Islands. Key brands within the Kona brand family are:

Kona core beers

- Longboard Island Lager ("Longboard"). Kona's top selling beer and flagship brand is a traditionally brewed lager with a delicate, slightly spicy hop aroma that is complimented by a fresh, malt-forward flavor and a smooth, refreshing finish.

- Fire Rock Pale Ale ("Fire Rock"). Fire Rock is a crisp, "Hawaiian Style" pale ale with pronounced citrus and floral hop aromas and flavors that are backed up by a generous malt profile.

Kona seasonal beers

- Koko Brown Ale ("Koko"). Koko is an American brown ale with a deep amber color and rich mahogany hues. This ale has a smoky, roasted nut aroma and flavor, with a coconut twist. Koko Brown Ale is Kona's spring seasonal.

- Pipeline Porter ("Pipeline"). Pipeline is smooth and dark, with a distinctive, roasty aroma and earthy flavor. This ale is brewed with fresh 100% Kona coffee to impart a rich complexity not found in many beers. Available fall and winter.

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- Wailua Wheat ("Wailua"). Wailua is a golden, sun-colored ale with a bright, citrusy flavor. This beer is brewed with a touch of tropical passion fruit to impart a slightly tart and crisp finish. Available late spring and summer.

Kona variety packs

- Kona Island Hopper and Big Kahuna Variety Packs. Kona offers two variety packs: Island Hopper variety 12-packs and Big Kahuna variety 24-packs. Both packages include the brewery's flagship Longboard Island Lager along with Fire Rock Pale Ale and then two of our Aloha Series seasonal offerings: Koko Brown, Wailua Wheat, and Pipeline Porter.

New Products and Brands

In an effort to stay current with consumer style and flavor preferences, we routinely analyze consumer trends and behavior, trends in other food and beverage segments, and our brand families and product offerings to identify beer styles or consumer taste preferences that appear to be under-served or not currently addressed. After identifying a potential new product offering, we will either tap into our brewing recipe library to determine if we have offered the targeted style either on a one-time basis or as a limited seasonal run or will use our pilot brewing system to create an experimental new beer. We may then offer this experimental new brew directly to consumers through on-premise test marketing at our own pubs and at exclusive retail sites. If the initial consumer reception of an experimental or new brew appears to meet the desired taste profile, we develop a brand identity to solidify the consumer perception of the product. We believe that our continued success is based on our ability to be attentive and responsive to consumer desires for new and distinctive tastes, and our capacity to meet these desires with original and novel taste profiles while maintaining consistently high product quality.

Contract Brewing

In order to profitably use excess capacity, we have entered into two contract brewing arrangements under which we produce beer in volumes and per specifications as designated by third parties. During 2011, we shipped 49,300 barrels under these contract brewing arrangements. We believe our relationships with our contract brewing clients are strong and we expect volumes to remain consistent in future periods.

Brewing Operations

Brewing Facilities

We use highly automated brewing equipment at our four production breweries and also operate a smaller, manual brewpub-style brewing system. Our breweries consist of the following:

- Oregon Brewery. Our Oregon Brewery is our largest capacity production brewery, consisting of a 230 barrel brewing system with an annual capacity of 455,000 barrels.

- Washington Brewery. Our Washington Brewery utilizes a 100 barrel brewing system and has an annual capacity of 220,000 barrels.

- New Hampshire Brewery. Our New Hampshire Brewery utilizes a 100 barrel brewing system and has an annual capacity of 215,000 barrels. It uses an anaerobic waste-water treatment facility that completes the process cycle.

- Hawaiian Brewery. Our Hawaiian Brewery, which was acquired with the KBC Merger, utilizes a 25 barrel brewing system and has an annual capacity of 10,000 barrels. During 2010, the Hawaiian Brewery installed a 229-kilowatt photovoltaic solar energy generating system to supply approximately 50 percent of its energy requirements through renewable energy.

- Rose Quarter Brewery. Our Rose Quarter Brewery maintains a 10 barrel pilot brewing system at the Rose Quarter sports arena in Portland, Oregon and is our smallest brewery.

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Packaging

We package our craft beers in bottles, kegs and, for the Hefeweizen brand, 5-liter steel cans. All of our production breweries, with the exception of the Hawaiian Brewery, have fully automated bottling and keg lines. The bottle filler at all of the breweries utilizes a carbon dioxide environment during bottling, ensuring that minimal oxygen is dissolved in the beer, extending the shelf life. During 2011, we launched new packaging for the Redhook brand family, including a unique glass bottle for all of the brands offered off premise. In February 2012, we added a small, manually operated canning line for our Kona Longboard Island Lager. We offer an assortment of packages to highlight the unique characteristics of each of our beers and to provide greater opportunities for customers to drink our beers in more locations and at more events and occasions, matching the active lifestyles and preferences of a greater number of our consumers.

Quality Control

We monitor production and quality control at all of our breweries, with central coordination at the Oregon Brewery. All of the breweries have an on-site laboratory where microbiologists and lab technicians supervise on-site yeast propagation, monitor product quality, test products, measure color and bitterness, and test for oxidation and unwanted bacteria. We also regularly utilize outside laboratories for independent product analysis. In addition, every batch of beer that we produce goes through a panel of internal testers (our taste panel) who ensure it meets our taste and profile standards.

Ingredients and Raw Materials

We currently purchase a significant portion of our malted barley from two suppliers and our premium-quality select hops, mostly grown in the Pacific Northwest, from competitive sources. We also periodically purchase small lots of hops from international sources, such as New Zealand and Western Europe, which we use to achieve a special hop character in certain beers. In order to ensure the supply of the hop varieties used in our products, we enter into supply contracts for our hop requirements. We believe that comparable quality malted barley and hops are available from alternate sources at competitive prices, although there can be no assurance that pricing would be consistent with our current arrangements. We currently cultivate our own yeast supply for certain strains and maintain a separate, secure supply in-house. We have access to multiple competitive sources for packaging materials, such as labels, six-pack carriers, crowns, cans and shipping cases.

Distribution

We are the only craft brewer in the U.S. to have a wholly aligned distribution network through our partnership with A-B. This partnership provides us seamless national distribution, which results in both a highly effective distribution presence in each market and distribution and administrative efficiencies. Our products are delivered to these retail outlets through this network of local distributors. Our beers are available for sale directly to consumers in draft and bottles at restaurants, bars and liquor stores, as well as in bottles at supermarkets, warehouse clubs, convenience stores and drug stores. We sell beer directly to consumers at our brew pubs and breweries.

Our products are distributed in all 50 states, pursuant to a master distributor agreement with A-B that allows us access to A-B's national distribution network. For additional information regarding our relationship with A-B, see "Relationship with A-B" below. A-B distributes beer throughout the United States through a network of more than 510 independently owned and operated wholesale distributors, most of whom are geographically contiguous, and 14 wholesale distributors owned and operated directly by A-B. According to industry sources, A-B's products accounted for 47.9% of total beer shipped by volume in the United States in 2011. Management believes that our competitors in the craft beer segment generally negotiate distribution relationships separately with distributors in each locality and, as a result, typically distribute through a variety of wholesalers representing differing national beer brands with uncoordinated territorial boundaries.

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In 2011 and 2010, we sold approximately 611,200 barrels and 574,900 barrels, respectively, to the wholesalers in A-B's distribution network through the A-B Distributor Agreement, accounting for 90.9% and 94.6%, respectively, of our shipment volume for the corresponding periods.

Sales and Marketing

We promote our products through a variety of means, including i) creating and executing a range of advertising programs; ii) training and educating wholesalers and retailers about our products; iii) promoting our name, product offerings and brands, and experimental beers at local festivals, venues and pubs; iv) selling our beers in the restaurants and pubs operated by us; and v) targeted discounting to create competitive advantage within the market place.

We advertise our products through an assortment of media, including television, radio, billboard, print and social media, including Facebook and Twitter, in key markets and by participating in co-operative programs with our distributors whereby our spending is matched by the distributor. We believe that the financial commitment by the distributor helps align the distributor's interests with ours, and the distributor's knowledge of the local market results in an advertising and promotion program that is targeted in a manner that will best promote our products.

Our breweries also play a significant role in increasing consumer awareness of our products and enhancing our image as a craft brewer. Many visitors take tours at our breweries and all of our production breweries have a retail restaurant or pub where our products are served. In addition, several of the breweries have meeting rooms that the public can rent for business meetings, parties and holiday events, and that we use to entertain and educate distributors, retailers and the media about our products. At our pubs, we also sell various items of apparel and memorabilia bearing our trademarks, which creates further awareness of our beers and reinforces our quality image.

To further promote retail bottled product sales and in response to local competitive conditions, we regularly recommend that wholesalers offer discounts to retailers in most of our markets. Distributors usually share in the cost of these price discounts.

Relationship with Anheuser-Busch, LLC

Exchange Agreement

We have an agreement with A-B (the "Exchange Agreement"), which entitles A-B to designate two members of our board of directors. A-B also generally has the right to have a designee on each committee of the board of directors, except where prohibited by law or stock exchange requirements, or with respect to a committee formed to review or determine transactions or proposed transactions between A-B and us. The Exchange Agreement also contains limitations on our ability to take certain actions without A-B's prior consent, including, but not limited to, our ability to issue equity securities or acquire or sell assets or stock, amend our Articles of Incorporation or bylaws, grant board representation rights, enter into certain transactions with affiliates, distribute our products in the United States other than through A-B or as provided in the A-B Distributor Agreement, or voluntarily delist or terminate our listing on the Nasdaq Stock Market.

Distributor Agreement

The A-B Distributor Agreement provides for the distribution of Widmer Brothers, Redhook, and Kona beers in all states, territories and possessions of the United States, including the District of Columbia and (except with respect to Kona beers) all U.S. military, diplomatic, and governmental installations in a U.S. territory or possession. Under the A-B Distributor Agreement, we granted A-B the right of first refusal to distribute our products, including any new products (other than new products that we acquire). We are responsible for marketing our products to A-B's distributors, as well as to retailers and consumers.

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The A-B Distributor Agreement has a term that expires on December 31, 2018, subject to automatic renewal for an additional ten-year period unless A-B provides written notice of non-renewal to us on or prior to June 30, 2018. The A-B Distributor Agreement is also subject to immediate termination, by either party, upon the occurrence of certain events as defined in the agreement, including the following:

- a material default by the other party in the performance of the A-B Distributor Agreement or any other agreement between the parties;
- certain bankruptcy and insolvency events; or
- any material misrepresentation made by the other party under or in the course of performance of the A-B Distributor Agreement.

Additionally, the A-B Distributor Agreement may be terminated by A-B, upon six months' prior written notice to us upon the occurrence of any of the following events:

- we engage in certain incompatible conduct that is not cured to A-B's satisfaction (at A-B's sole discretion) within 30 days. Incompatible conduct is defined as any act or omission that, in A-B's opinion, damages the reputation or image of A-B or the brewing industry;
- any A-B competitor or affiliate thereof acquires 10% or more of our outstanding equity securities, and that entity designates one or more persons to our board of directors;
- our current chief executive officer ceases to function in that role or is terminated, and a satisfactory successor, in A-B's opinion, is not appointed within six months;
- we are merged or consolidated into or with any other entity or any other entity merges or consolidates into or with us without A-B's prior approval; or
- A-B, its subsidiaries, affiliates, or parent, incur any obligation or expense as a result of a claim asserted against them by or in our name, its affiliates or shareholders, and we do not reimburse and indemnify A-B and its corporate affiliates on demand for the entire amount of the obligation or expense.

As of both December 31, 2011 and 2010, A-B owned approximately 32.2% of our outstanding common stock.

Fees

We pay fees to A-B in connection with the sale of our products, including margin fees, invoicing, staging and cooperage handling fees, inventory manager fees and a wholesaler support center ("WSC") fees.

In instances when we ship our products to A-B's WSC rather than directly to the wholesaler, A-B's WSC assists us by consolidating small wholesaler orders with orders of other A-B products prior to shipping to the wholesaler.

See Note 19 of Notes to Consolidated Financial Statements for additional information.

Seasonality

Our sales generally reflect a degree of seasonality, with the first and fourth quarters historically exhibiting low sales levels relative to the second and third quarters. Accordingly, our results for any particular quarter are not likely to be indicative of the results to be achieved for the full year.

Competition

We compete in the craft brewing market as well as in the much larger specialty beer market, which encompasses producers of imported beers, major national brewers that have introduced fuller-flavored products, and large spirit companies and national brewers that produce flavored alcohol beverages. Beyond the beer market, craft brewers have also faced increasing competition from producers of wines and spirits.

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Competition within the domestic craft beer segment and the specialty beer market is based on product quality, taste, consistency and freshness, ability to differentiate products, promotional methods and product support, marketing, transportation costs, distribution coverage, local appeal and price.

The craft beer segment is increasingly competitive due to the proliferation of small craft brewers, including contract brewers, and the large number of products offered by such brewers. Craft brewers have also encountered more competition as their peers expand distribution. Competition also varies by regional market. Depending on the local market preferences and distribution, we have encountered strong competition from microbreweries, regional specialty brewers and several national craft brewers. Because of the large number of participants and number of different products offered in this segment, the competition for bottled product placements and especially for draft beer placements has intensified. Although certain of these competitors distribute their products nationally and may have greater financial and other resources than we have, we believe that we possess certain competitive advantages, including our broad array of brand offerings within our three brand families and the scale of our production breweries.

We also compete against producers of imported brands, such as Heineken, Corona Extra and Guinness. Most of these foreign brewers have significantly greater financial resources than we have. Although imported beers currently account for a greater share of the U.S. beer market than craft beers, we believe that craft brewers possess certain competitive advantages over some importers, including lower transportation costs, no importation costs, proximity to and familiarity with local consumers, a higher degree of product freshness, eligibility for lower federal excise taxes and absence of currency fluctuations.

In response to the growth of the craft beer segment, most of the major domestic national brewers have introduced fuller-flavored beers, including well-funded significant product launches in the wheat category. While these product offerings are intended to compete with craft beers, many of them are brewed according to methods used by these brewers in their other product offerings. The major national brewers have significantly greater financial resources than us and have access to a greater array of advertising and marketing tools to create product awareness of these offerings. Although increased participation by the major national brewers increases competition for market share and can heighten price sensitivity within the craft beer segment, we believe that their participation tends to increase advertising, distribution and consumer education and awareness of craft beers, and thus may ultimately contribute to further growth of this industry segment.

In the past several years, several major distilled spirits producers and national brewers have introduced flavored alcohol beverages. Products such as Smirnoff Ice, Bacardi Silver and Mike’s Hard Lemonade have captured sizable market share in the higher-priced end of the malt beverage industry. We believe sales of these products, along with strong growth in the imported and craft beer segments of the malt beverage industry, contributed to an increase in the overall U.S. alcohol market. These products are particularly popular in certain regions and markets in which we sell our products.

Competition for consumers of craft beers has also come from wine and spirits. This growth appears to be attributable to competitive pricing, television advertising, increased merchandising and increased consumer interest in wine and spirits. Recently, the wine industry has been aided, on a limited basis, by its ability to sell outside of the three-tier system, allowing sales to be made directly to the consumer. While the craft beer segment competes with wine and spirits, it also benefits from many of the same advantages enjoyed by wine and spirit producers. These include consumers who allow themselves affordable luxuries in the form of high quality alcoholic beverages.

A significant portion of our sales continues to be in the Pacific Northwest and in California, which we believe are among the most competitive craft beer markets in the United States, both in terms of number of participants and consumer awareness. We believe that these areas offer significant competition for our products, not only from other craft brewers but also from the growing wine market and from flavored alcohol beverages. Our recent marketing efforts have been focused on creating appealing new brands and better communicating the attributes of our stable of existing beers, highlighting and strengthening the identities to better match the preferences and lifestyles of a greater number of consumers. We believe that our broad array of beers and brands enables us to offer an assortment of flavors and experiences that appeal to more people.

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Segment and Enterprise-Wide Information

See Note 13 of Notes to Consolidated Financial Statements included in Part II, Item 8 of this Annual Report on Form 10-K for the required segment and enterprise-wide information.

Regulation

Our business is highly regulated at federal, state and local levels. Various permits, licenses and approvals necessary for our brewery and pub operations and the sale of alcoholic beverages are required from a number of agencies, including the U.S. Treasury Department, the Alcohol and Tobacco Tax and Trade Bureau ("TTB"), the U.S. Department of Agriculture, the U.S. Food and Drug Administration, state alcohol regulatory agencies, and state and local health, sanitation, safety, fire and environmental agencies. In addition, the beer industry is subject to substantial federal and state excise taxes, although smaller brewers producing less than two million barrels annually, including us, benefit from favorable treatment.

We operate our breweries under federal licensing requirements imposed by the TTB. The TTB requires the filing of a "Brewer's Notice" upon the establishment of a commercial brewery and the filing of an amended Brewer's Notice any time there is a material change in the brewing or warehousing locations, brewing or packaging equipment, brewery ownership, or officers or directors. Our operations are subject to audit and inspection by the TTB at any time.

Management believes that we currently have all of the licenses, permits and approvals required for our current operations. Existing permits or licenses could be revoked if we fail to comply with the terms of such permits or licenses and additional permits or licenses may be required in the future for our current operations or as a result of expanding our operations in the future.

The U.S. federal government currently levies an excise tax of $18 per barrel on beer sold for consumption in the United States; however, brewers that produce less than two million barrels annually are taxed at $7 per barrel on the first 60,000 barrels shipped, with shipments above this amount taxed at the normal rate. Certain states also levy excise taxes on alcoholic beverages. It is possible that excise taxes may be increased in the future by the federal government or any state government or both. In the past, increases in excise taxes on alcoholic beverages have been considered in connection with various governmental budget-balancing or funding proposals.

Federal and State Environmental Regulation
Our brewing operations are subject to environmental regulations and local permitting requirements and agreements regarding, among other things, air emissions, water discharges and the handling and disposal of hazardous wastes. While we have no reason to believe the operation of our breweries violate any such regulation or requirement, if such a violation were to occur, or if environmental regulations were to become more stringent in the future, we could be adversely affected.

Dram Shop Laws
The serving of alcoholic beverages to a person known to be intoxicated may, under certain circumstances, result in the server being held liable to third parties for injuries caused by the intoxicated customer. Our restaurants and pubs have addressed this issue by maintaining reasonable hours of operation and routinely performing training for personnel.

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Trademarks

We have obtained U.S. trademark registrations for our numerous products, including our proprietary bottle designs. Trademark registrations generally include specific product names, marks and label designs. The Widmer Brothers, Redhook, and Kona Brewing marks and certain other marks are also registered in various foreign countries. We regard our Widmer Brothers, Redhook, Kona Brewing and other trademarks as having substantial value and as being an important factor in the marketing of our products. We are not aware of any infringing uses that could materially affect our current business or any prior claim to the trademarks that would prevent us from using such trademarks in our business. Our policy is to pursue registration of our trademarks in our markets whenever possible and to oppose vigorously any infringement of our trademarks.

Employees

At December 31, 2011, we employed approximately 675 people, including 330 employees in the pubs, restaurant and retail stores, 180 employees in production, 120 employees in sales and marketing and 45 employees in corporate and administration. The pubs and restaurants have 195 part-time employees and 20 seasonal or temporary employees, both of which are included in the totals above. None of our employees are represented by a union or employed under a collective bargaining agreement. We believe our relations with our employees to be good.

Available Information

Our Internet address is www.craftbrew.com. There we make available, free of charge, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and any amendments to those reports, as soon as reasonably practicable after we electronically file such material with or furnish them to the Securities and Exchange Commission ("SEC"). Our SEC reports can be accessed through the investor relations section of our Web site. The information found on our Web site is not part of this or any other report we file with or furnish to the SEC.

Item 1A. Risk Factors

If we are unable to gauge trends and react to changing consumer preferences in a timely manner, our sales and market share will decrease.
The costs and management attention involved in maintaining an innovative brand portfolio have been, and are expected to continue to be, significant. If we have not gauged consumer preferences correctly, or are unable to maintain consistently high quality beers as we develop new brands, our overall brand image may be damaged. If this were to occur, our future sales, results of operations and cash flows would be adversely affected.

Increased competition could adversely affect sales and results of operations.
We compete in the highly competitive craft brewing market, as well as in the much larger specialty beer category, which includes the imported beer segment and fuller-flavored beer offered by major national brewers. We also face increasing competition from producers of wine, spirits and flavored alcohol beverages offered by the larger spirit producers and national brewers. Increased competition could cause our future sales and results of operations to be adversely affected.

Our information systems may experience an interruption or breach in security.
We rely on computer information systems in the conduct of our business. We have policies and procedures in place to protect against and reduce the occurrence of failures, interruptions, or breaches of security of these systems. However, there can be no assurances that these policies and procedures will eliminate the occurrence of failures, interruptions or breaches of security or that they will adequately restore our systems or minimize any such events. The occurrence of a

failure, interruption or breach of security of our computer information systems could result in loss of intellectual property, delays in our production, loss of critical information, or other events, any of which could harm our future sales or operating results.

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Our business is sensitive to reductions in discretionary consumer spending.
Consumer demand for luxury or perceived luxury goods, including craft beer, is sensitive to downturns in the economy and the corresponding impact on discretionary spending. There is no assurance that the craft brewing segment will continue to experience growth in future periods. Changes in discretionary consumer spending or consumer preferences brought about by factors such as perceived or actual general economic conditions, job losses and the resultant rising unemployment rate, perceived or actual disposable consumer income and wealth, and changes in consumer confidence in the economy, could significantly reduce customer demand for craft beer in general, and the products we offer specifically. Furthermore, our consumers may choose to replace our products with the fuller-flavored national brands or other more affordable, although lower quality, alternatives available in the market. Any such decline in consumption of our products would likely have a significant negative impact on our operating results.

We are dependent upon our continuing relationship with Anheuser-Busch, LLC and the current distribution network.
Substantially all of our products are sold and distributed through A-B's distribution network. If the A-B Distributor Agreement were terminated, we would be faced with a number of operational tasks, including implementing information technology systems to manage our supply chain, order management and logistics, establishing and maintaining direct contracts with the existing wholesaler network or negotiating agreements with replacement wholesalers on an individual basis, and enhancing our credit evaluation, billing, accounts receivable, and regulatory processes. Such an undertaking would require significant effort and substantial time to complete, during which the distribution of our products could be impaired. While we believe that the total one-time and recurring costs associated with such an undertaking may be lower than the total fees paid under the current arrangement with A-B, there can be no assurance that costs of such an undertaking would not exceed the total fees currently paid to A-B.

Other products developed or introduced by A-B or its parent may reduce wholesaler attention and financial resources committed to our products. There is no assurance that we will be able to successfully compete in the marketplace against other A-B supported products or beers produced by other companies. A reduction in the level of A-B's support of our products could cause our sales and results of operations to be adversely affected.

We are dependent on our wholesalers for the sale of our products.
Although substantially all of our products are sold and distributed through A-B, we continue to rely heavily on wholesalers, most of which are independent, for the sale of our products to retailers. Any disruption in the ability of the wholesalers, A-B, or us to distribute products efficiently due to any significant operational problems, such as wide-spread labor union strikes or the loss of a major wholesaler as a customer, could hinder our ability to get our products to retailers and could have a material adverse impact on our sales, results of operations and cash flows.

In 2008, A-B modified the restrictions around its program associated with its decade-long policy of rewarding financial incentives to those wholesalers and distributors that did not distribute malt beverage products other than those within the A-B brand family or affiliated entities, including our products. The modified program now allows A-B wholesalers to carry a small volume of competitive brands without foregoing all of the financial incentives associated with its incentive program. Media reports indicated that at the height of this program, 70 percent of A-B sales were made through wholesalers and distributors carrying only the A-B and alliance brands, but this amount has steadily declined to its present level of under 60 percent. Under the current version of the program, a second tier is available for those wholesalers who may be permitted to carry up to three percent of their volume in competitive beer brands and non-alcohol brands while retaining some of the financial benefits of the incentive program. In the opinion of our management, the modification has led to increased direct competition for us for the attention and focus of A-B wholesalers, as many specialty, regional and local craft brewers are now using the same distributors through which we market our products, and this could have a material impact on our sales, results of operations and cash flows.

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Our agreements with A-B place limitations on our ability to engage in or reject certain transactions, including acquisitions and changes of control.
The Exchange Agreement requires us to obtain the consent of A-B prior to taking certain actions. The practical effect of these restrictions is to grant A-B the ability to veto certain transactions that management may believe to be in the best interest of our shareholders, including our expansion through acquisitions of other craft brewers or new brands, mergers with other brewing companies or distribution of our products outside of the United States. As a result, our financial condition, results of operations, cash flows and the trading price of our common stock may be adversely affected.

A-B holds certain rights affecting corporate governance and significant corporate transactions. As of December 31, 2011, A-B owns approximately 32.2% of our outstanding common stock and, under the Exchange Agreement, has the right to appoint two designees to our board of directors. A-B also generally has the contractual right to have a designee on each of the board committees except where prohibited by law or stock exchange requirements, and in those cases an A-B designee acts as an observer. As a result, A-B may have significant influence, particularly with respect to matters requiring approval of our shareholders. This could limit the ability of other shareholders to influence corporate matters and may have the effect of delaying or preventing a third party from acquiring control of us. In addition, A-B may have actual or potential interests that differ from our other shareholders.

We are dependent on certain A-B information systems and operational support.
We rely on components of A-B's supply-chain and financial information systems to support our operations, particularly for the distribution of and payment for our products. As the maintenance and upkeep of these systems is under A-B's control, revisions to these systems and efforts to deal with any disruptions will be made at A-B's direction, which may result in delays in the restoration of systems critical to our operations. Any disruption in these critical information services could have a material adverse effect on our financial condition, results of operations and cash flows. We may also incur incremental costs associated with changes to either A-B's information systems, operational support or the A-B distribution network, which could have a material adverse effect on our financial condition, results of operations and cash flows.

Operating breweries at production levels substantially below their current designed capacities could negatively impact our financial results.
As of December 31, 2011, the annual working capacity of our breweries was approximately 900,000 barrels. Due to many factors, including seasonality and production schedules of various draft products and bottled products and packages, actual production capacity will rarely, if ever, approach full working capacity. We believe that capacity utilization of the breweries will fluctuate throughout the year, and even though we expect that capacity of our breweries will be efficiently utilized during periods when our sales are strongest, there likely will be periods when the capacity utilization will be lower. If we experience contraction in our sales volumes, the resulting excess capacity and unabsorbed overhead will have an adverse effect on our gross margins, operating cash flows and overall financial performance. We periodically evaluate whether we expect to recover the costs of our production breweries over the course of their useful lives. If facts and circumstances indicate that the carrying value of these long-lived assets may be impaired, an evaluation of recoverability will be performed by comparing the carrying value of the assets to projected future undiscounted cash flows along with other quantitative and qualitative analyses. If we determine that the carrying value of such assets does not appear to be recoverable, we will recognize an impairment loss by a charge against current operations, which could have a material adverse effect on our results of operations.

Our sales are concentrated in the Pacific Northwest and California.
Nearly two-thirds of our sales in 2011 were in the Pacific Northwest and California and, consequently, our future sales may be adversely affected by changes in economic and business conditions within these areas. We also believe these regions are among the most competitive craft beer markets in the United States, both in terms of number of market participants and consumer awareness. The Pacific Northwest and California offer significant competition to our

products, not only from other craft brewers but also from wine producers and flavored alcohol beverages.

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The craft beer business is seasonal in nature, and we are likely to experience fluctuations in results of operations and financial condition.
Sales of craft beer products are somewhat seasonal, with the first and fourth quarters historically being lower and the rest of the year generating stronger sales. Our sales volume may also be affected by weather conditions and selling days within a particular period. Therefore, the results for any given quarter will likely not be indicative of the results that may be achieved for the full fiscal year. If an adverse event such as a regional economic downturn or poor weather conditions should occur during the second and third quarters, the adverse impact to our revenues would likely be greater as a result of the seasonal business.

Changes in consumer preferences or public attitudes about alcohol could decrease demand for our products.
If consumers were unwilling to accept our products or if general consumer trends caused a decrease in the demand for beer, including craft beer, it would adversely impact our sales and results of operations. If the markets for wine, spirits or flavored alcohol beverages continue to grow, this could draw consumers away from the beer industry in general and our products specifically and have an adverse effect on our sales and results of operations. Further, the alcoholic beverage industry has become the subject of considerable societal and political attention in recent years due to increasing public concern over alcohol-related social problems, including drunk driving, underage drinking and health consequences from the misuse of alcohol. As an outgrowth of these concerns, the possibility exists that advertising by beer producers could be restricted, that additional cautionary labeling or packaging requirements might be imposed or that there may be renewed efforts to impose, at either the federal or state level, increased excise or other taxes on beer sold in the United States. If beer in general were to fall out of favor among domestic consumers, or if the domestic beer industry were subjected to significant additional governmental regulation, it would likely have a significant adverse impact on our financial condition, operating results and cash flows.

We are dependent upon the services of our key personnel.
If we lose the services of any members of senior management or key personnel for any reason, we may be unable to replace them with qualified personnel, which could have a material adverse effect on our operations. Additionally, the loss of Terry Michaelson as our chief executive officer, and the failure to find a replacement satisfactory to A-B, would be a default under the A-B Distributor Agreement.

Our gross margin may fluctuate.
Future gross margin may fluctuate and even decline as a result of many factors, including: product pricing levels; sales mix between draft and bottled product sales and within the various bottled product packages; level of fixed and semi-variable operating costs; level of production at our breweries in relation to current production capacity; availability and prices of raw materials, production inputs such as energy, and packaging materials; rates charged for freight; and federal and state excise taxes. The high percentage of fixed and semi-variable operating costs causes our gross margin to be particularly sensitive to relatively small changes in sales volume.

We are subject to governmental regulations affecting our breweries and pubs.
Federal, state and local laws and regulations govern the production and distribution of beer, including permitting, licensing, trade practices, labeling, advertising and marketing, distributor relationships and various other matters. A variety of federal, state and local governmental authorities also levy various taxes, license fees and other similar charges and may require bonds to ensure compliance with applicable laws and regulations. Certain actions undertaken by us may cause the Alcohol and Tobacco Tax and Trade Bureau or any particular state or jurisdiction to revoke its license or permit, restricting our ability to conduct business. One or more regulatory authorities could determine that we have not complied with applicable licensing or permitting regulations or have not maintained the approvals necessary for us to conduct business within our jurisdiction. If licenses, permits or approvals necessary for our brewery or pub operations were unavailable or unduly delayed, or if any permits or licenses that we hold were to be revoked, our ability to conduct business may be disrupted, which would have a material adverse effect on our financial condition, results of operations and cash flows.

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We believe that we currently have all of the licenses, permits and approvals required for our current operations. However, we do business in almost every state through the A-B distribution network, and for many of these states, we rely on the licensing, permitting and approvals maintained by A-B. If a state or a number of states required us to obtain our own licensing, permitting or approvals to operate within the state's boundaries, a combination of events may occur, including a disruption of sales or significant increases in compliance costs. If licenses, permits or approvals not previously required for the sale of our malt beverage products were to be required, the ability to conduct our business could be disrupted, which may have a material adverse effect on our financial condition, results of operations and cash flows.

An increase in excise taxes could adversely affect our financial condition and results of operations.
The U.S. federal government currently levies an excise tax of $18 per barrel on beer sold for consumption in the United States; however, brewers that produce less than two million barrels annually are taxed at $7 per barrel on the first 60,000 barrels shipped, with the remainder of the shipments taxed at the normal rate. Individual states that we operate in also impose excise taxes on beer and other alcohol beverages in varying amounts, which have been subject to change. Federal and state legislators routinely consider various proposals to impose additional excise taxes on the production of alcoholic beverages, including beer. Any such increases in excise taxes, if enacted, would adversely affect our financial condition, results of operations and cash flows.

Changes in state laws regarding distribution arrangements may adversely impact our operations. States in which we have a significant sales presence may enact legislation that significantly alters the competitive environment for the beer industry. Any change in the competitive environment in those states could have an adverse effect on our future sales and results of operations and may impact the financial stability of wholesalers on which we rely.

We may experience a shortage of kegs necessary to distribute draft beer.
We distribute our draft beer in kegs that are owned by us as well as leased from a third-party vendor, and, on a limited basis, from A-B. During periods when we experience stronger sales, we may need to rely on kegs leased from A-B and the third-party vendor to address the additional demand. If shipments of draft beer increase, we may experience a shortage of available kegs to fill sales orders. If we cannot meet our keg requirements through either lease or purchase, we may be required to delay some draft shipments. Such delays could have an adverse impact on sales and relationships with wholesalers and A-B. We may also decide to pursue other alternatives for leasing or purchasing kegs, but there is no assurance that we will be successful in securing additional kegs.

We are dependent on certain suppliers for key raw materials, packaging materials and production inputs.
Although we seek to maintain back-up and alternative suppliers for all key raw materials and production inputs, we are reliant on certain third parties for key raw materials, packaging materials and utilities. Any disruption in the willingness or ability of these third parties to supply these critical components could hinder our ability to continue production of our products, which could have a material adverse impact on our financial condition, results of operations and cash flows.

Loss of income tax benefits could negatively impact our results of operations.
As of December 31, 2011, our deferred tax assets were primarily comprised of federal net operating losses ("NOLs") of $4.5 million, or $1.5 million tax-effected; state NOL carryforwards of $129,000 tax-effected; and federal and state alternative minimum tax credit carryforwards of $726,000 tax-effected. The ultimate realization of deferred tax assets is dependent upon generating taxable income during the periods in which those temporary differences become deductible. To the extent that we are unable to generate adequate taxable income in future periods, we may be required to record a valuation allowance to provide for potentially expiring NOLs or other deferred tax assets. Any such allowance would generally be charged to earnings in the period of increase. In addition, as NOLs are utilized, the potential for audit by federal and state jurisdictions will increase. The NOLs generated by us in 1997 through 2003 will be used on the 2011 tax return, which means these NOLs can be audited. An audit of these NOLs could be time

consuming and difficult given their age.

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A small number of shareholders hold a significant ownership percentage of the Company and uncertainty over their continuing ownership plans could cause the market price of our common stock to decline.
As noted above, A-B has a significant ownership stake in us. In addition, the founders of Widmer Brothers Brewing Company ("WBBC") and their close family members own approximately 3.4 million shares, or 18.0%, of our common stock. Collectively, these two groups own 50.2% of our equity. All of these shares are available for sale in the public market, subject to volume, manner of sale and other limitations under Rule 144 in the case of shares held by shareholders who are affiliates of us. Such sales in the public market or the perception that such sales could occur may cause the market price of our common stock to decline.

We do not intend to pay and are limited in our ability to declare or pay dividends; accordingly, shareholders must rely on stock appreciation for any return on their investment in us.
We do not anticipate paying cash dividends. Further, under our loan agreement with Bank of America ("BofA"), we are not permitted to declare or pay a dividend without BofA's prior consent. As a result, only appreciation of the price of our common stock will provide a return to shareholders. Investors seeking cash dividends should not invest in our common stock.

The fair value of our intangible assets, including goodwill, may become impaired.
As a result of the KBC Merger, we have recognized a significant increase in our total intangible assets, including goodwill. As of December 31, 2011, we had $30.1 million in an assortment of intangible assets, on a net basis, which represented nearly 19% of our total assets. If any circumstances were to occur, such as economic recession or other factors causing a reduction in consumer demand, or for any other reason we were to experience a significant decrease in sales growth, which had a negative impact on our estimated cash flows associated with these assets, our analyses of these assets may conclude that a decrease in the fair value of these assets occurred. If this were to occur, we would be required to recognize a potentially significant loss on impairment of these assets. Any such impairment loss would be charged against current operations in the period of change.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We own and operate four highly-automated, small-batch breweries: the Hawaiian Brewery, the New Hampshire Brewery, the Oregon Brewery and the Washington Brewery, as well as a small, manual brewpub-style brewing system at the Rose Quarter Brewery in Portland, Oregon. We lease the sites upon which the Hawaiian Brewery, the New Hampshire Brewery, and the Rose Quarter Brewery are located, in addition to our office space and warehouse locations in Portland, Oregon for our corporate, administrative and sales functions. These operating leases expire at various times between 2012 and 2047. Certain of these leases are with related parties. See Notes 18 and 19 of Notes to Consolidated Financial Statements included elsewhere herein for further discussion regarding these arrangements.

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Certain information regarding our production breweries is as follows (in thousands of barrels):

Production Breweries	Square Footage	Current Annual Capacity	Estimated December 31, 2012 Annual Capacity	Maximum Annual Capacity
Oregon Brewery	185,000	455	645	650
Washington Brewery	128,000	220	220	280
New Hampshire Brewery	125,000	215	215	280
Hawaiian Brewery	11,000	10	10	10
		900	1,090	1,220

As of December 31, 2011, the total capacity of all our breweries was approximately 900,000 barrels annually. As a result of adding fermentation capacity and modifying our brewing schedules, we expect the total annual capacity of all of our breweries to increase to approximately 1,090,000 barrels by the end of 2012 based on our current product mix. Combined, our breweries have the potential to reach 1,220,000 barrels in annual production capacity when fully optimized based on the currently available space and current product mix.

Substantially all of the personal property and the real properties associated with the Oregon Brewery and the Washington Brewery secure our loan agreement with BofA. See Note 10 of Notes to Consolidated Financial Statements included elsewhere herein.

Item 3. Legal Proceedings

We are involved, from time to time, in claims, proceedings and litigation arising in the normal course of business. We believe that, to the extent that any pending or threatened litigation involving us or our properties exists, such litigation will not likely have a material adverse effect on our financial condition or results of operations.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock trades on the NASDAQ Stock Market ("NASDAQ") under the trading symbol HOOK. The table below sets forth, for the fiscal quarters indicated, the reported high and low sale prices of our common stock, as reported on the NASDAQ:

2010	High	Low
Quarter 1	$ 2.73	$ 2.16
Quarter 2	5.15	2.31
Quarter 3	9.94	4.40
Quarter 4	8.27	6.01

2011	High	Low
Quarter 1	$ 9.59	$ 6.96
Quarter 2	10.17	8.10

Quarter 3	8.95	5.31
Quarter 4	7.22	5.08

We had 677 common shareholders of record as of March 5, 2012.

We have not declared or paid any dividends during our existence. Under the terms of our loan agreement with BofA, we may not declare or pay dividends without BofA's consent. We anticipate that, for the foreseeable future, all earnings will be retained for the operation and expansion of our business and that we will not pay cash dividends. The payment of dividends, if any, in the future, will be at the discretion of our Board of Directors and will depend upon, among other things, future earnings, capital and operating requirements, restrictions in future financing agreements, our general financial condition and general business conditions.

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Equity Compensation Plans

Information regarding securities authorized for issuance under equity compensation plans is included in Item 12 of this Form 10-K.

Recent Sales of Unregistered Securities

None.

Issuer Purchases of Equity Securities

We did not repurchase any of our common stock during the fourth quarter of 2011.

Stock Performance Graph

The following line-graph presentation compares cumulative five-year shareholder returns on an indexed basis, assuming a $100 initial investment and reinvestment of dividends, of (a) Craft Brew Alliance, Inc., (b) a broad-based equity market index and (c) an industry-specific index. The broad-based market index used is the NASDAQ Composite Index and the industry-specific index used is the S&P 500 Beverages Index.

	Base Period	Indexed Returns Year Ended				
Company/Index	12/31/06	12/31/07	12/31/08	12/31/09	12/31/10	12/31/11
Craft Brew Alliance, Inc.	$100.00	$127.88	$23.08	$46.15	$142.12	$115.77
NASDAQ Composite	100.00	109.81	65.29	93.95	109.84	107.86
S&P 500 Beverages Index	100.00	120.72	96.55	116.09	133.09	139.14

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Item 6. Selected Financial Data

The selected consolidated financial data below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and notes thereto included elsewhere in this Form 10-K.

In thousands, except per share amounts	Year Ended December 31,				
Statement of Operations Data	2011	2010	2009	2008	2007
Net sales(1)	$149,197	$131,731	$124,713	$79,761	$41,470
Cost of sales	104,011	98,064	97,230	65,646	36,785
Gross profit	$45,186	$33,667	$27,483	$14,115	$4,685
Selling, general and administrative expenses	$39,742	$29,938	$24,911	$19,894	$8,257
Loss on impairment of assets(2)	$-	$-	$-	$30,589	$-
Operating income (loss)	$5,444	$3,170	$2,347	$(36,761)	$(1,330)
Gain on sale of equity interest in Fulton Street Brewery, LLC	$10,432	$-	$-	$-	$-
Income before provision (benefit) for income taxes	$15,692	$2,786	$1,073	$(37,655)	$(1,115)
Provision (benefit) for income taxes	6,041	1,100	186	(4,377)	(176)
Net income (loss)	$9,651	$1,686	$887	$(33,278)	$(939)
Basic and diluted net income (loss) per share	$0.51	$0.10	$0.05	$(2.63)	$(0.11)
Shares used in basic per share calculations	18,834	17,523	17,004	12,660	8,331
Shares used in diluted per share calculations	18,931	17,568	17,041	12,660	8,331

	December 31,				
	2011	2010	2009	2008	2007
Balance Sheet Data					
Cash and cash equivalents	$795	$164	$11	$11	$5,527
Working capital (deficit)	2,327	(4,435)	(2,527)	(927)	5,714
Total assets	158,908	158,266	141,585	147,805	71,390
Current portion of long-term debt and capital leases	596	2,460	1,481	1,394	15
Long-term debt and capital leases, net of current portion	13,188	24,675	24,685	31,834	31
Other long-term obligations	16,261	11,388	8,210	8,082	1,988
Shareholders' equity	104,509	94,196	80,632	79,281	60,080

(1) The increase in net sales in 2009 compared to 2008 and in 2008 compared to 2007 was primarily due to the merger with Widmer Brothers Brewing Company, which occurred July 1, 2008.

(2) Loss on impairment of assets in 2008 included a $22.7 million charge for total impairment of goodwill, a $6.5 million charge for the partial write-down of trademarks associated with the Widmer brand and a $1.4 million charge for the partial write down of equity-method investments.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

Craft Brew Alliance is the union of three unique pioneering craft brewers:

- Redhook Ale Brewery founded by Gordon Bowker and Paul Shipman in 1981 in Seattle, Washington;
- Widmer Brothers Brewery founded by brothers Kurt and Rob Widmer in 1984 in Portland, Oregon; and
- Kona Brewing Co. founded by father and son team Cameron Healy and Spoon Khalsa in 1994 in Kona, Hawaii.

Since our formation, we have focused our business activities on satisfying consumers through the brewing, marketing and selling of high-quality craft beers in the United States. Today, as an independent craft brewer, we possess several distinct and ownable advantages, unique in the craft beer category. These advantages are rooted and leveraged through the combination of our innovative quality craft beers, the strength of our distinct, authentic brand portfolio, our seamless national distribution, our financial capabilities as a public company, our national sales and marketing reach, our owned brew pubs and our bi-coastal breweries.

We operate in two segments: Beer Related operations and Pubs and Other. Beer Related operations include the brewing and sale of craft beers from our five breweries: Widmer Brothers and the Rose Quarter in Portland, Oregon; two Redhook, one in Woodinville, Washington and one in Portsmouth, New Hampshire; and Kona in Kona, Hawaii. Pubs and Other operations primarily include our five pubs, four of which are located adjacent to our Beer Related operations.

We proudly brew our Widmer Brothers, Redhook and Kona beers in each of our three company-owned mainland production breweries that are located in Portsmouth, New Hampshire (the "New Hampshire Brewery"); Portland, Oregon (the "Oregon Brewery"), which is our largest brewery; and in the Seattle suburb of Woodinville, Washington (the "Washington Brewery"). Our brewery located in Kailua-Kona, Hawaii (the "Hawaiian Brewery") brews our Kona branded beers. We also own and operate a small manual style brewery, primarily used for small batch production and innovative brews, at the Rose Quarter in Portland, Oregon. We sell our beers primarily to wholesalers via a Master Distributor Agreement ("A-B Distributor Agreement") with Anheuser-Busch, LLC ("A-B"). Redhook and Widmer Brothers beers are distributed in all 50 states and Kona beers are distributed in 29 states. Separate from our A-B wholesalers, we maintain an independent sales and marketing organization complete with resources across the key functions of brand management, field marketing, field sales, and national retail sales.

Following is a summary of our financial results:

	Net Sales	Net Income	Number of Barrels Sold
2011	$ 149.2 million	$ 9.7 million	672,600
2010	$ 131.7 million	$ 1.7 million	607,800
2009	$ 124.7 million	$ 0.9 million	587,500

The comparability of our results for 2011 relative to the results for 2010 and 2009 is significantly impacted by the merger with Kona Brewing Co., Inc. ("KBC"), which closed October 1, 2010 ("KBC Merger"), and by the sale of our equity interest in Fulton Street Brewery, LLC ("FSB") during the second quarter of 2011. See Notes 7 and 8 of Notes to Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for more detailed information.

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Results of Operations

The following table sets forth, for the periods indicated, certain information from our Consolidated Statements of Income expressed as a percentage of net sales(1):

	Year Ended December 31,		
	2011	2010	2009
Sales	107.9 %	106.9 %	106.9 %
Less excise tax	7.9	6.9	6.9
Net sales	100.0	100.0	100.0
Cost of sales	69.7	74.4	78.0
Gross profit	30.3	25.6	22.0
Selling, general and administrative expenses	26.6	22.7	20.0
Merger related expenses	-	0.4	0.2
Operating income	3.6	2.4	1.9
Income from equity method investments	0.5	0.6	0.4
Gain on sale of Fulton Street Brewery	7.0	-	-
Interest expense	(0.6)	(1.1)	(1.7)
Interest and other income, net	-	0.2	0.3
Income before income taxes	10.5	2.1	0.9
Income tax provision	4.0	0.8	0.1
Net income	6.5 %	1.3 %	0.7 %

(1) Percentages may not sum due to rounding.

Segment Information

Net sales, gross profit and gross margin information by segment was as follows (dollars in thousands):

	Year Ended December 31,		
	Beer	Pubs	
2011	Related	and Other	Total
Net sales	$ 125,531	$ 23,666	$ 149,197
Gross profit	$ 41,372	$ 3,814	$ 45,186
Gross margin	33.0 %	16.1 %	30.3 %
2010			
Net sales	$ 117,563	$ 14,168	$ 131,731
Gross profit	$ 31,607	$ 2,060	$ 33,667
Gross margin	26.9 %	14.5 %	25.6 %
2009			
Net sales	$ 113,439	$ 11,274	$ 124,713
Gross profit	$ 25,827	$ 1,656	$ 27,483
Gross margin	22.8 %	14.7 %	22.0 %

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Sales by Category

The following tables set forth a comparison of sales by category (dollars in thousands):

Sales by Category	Year Ended December 31, 2011	2010	Dollar Change	% Change
A-B and A-B related	$ 130,137	$ 114,296	$ 15,841	13.9 %
Pubs and Other(1)	23,666	14,168	9,498	67.0 %
Contract brewing and other beer related	7,197	2,542	4,655	183.1 %
Alternating proprietorship	-	9,846	(9,846)	(100.0)%
Gross sales	161,000	140,852	20,148	14.3 %
Excise taxes	(11,803)	(9,121)	(2,682)	29.4 %
Net sales	$ 149,197	$ 131,731	$ 17,466	13.3 %

Sales by Category	Year Ended December 31, 2010	2009	Dollar Change	% Change
A-B and A-B related	$ 114,296	$ 110,840	$ 3,456	3.1 %
Pubs and Other(1)	14,168	11,274	2,894	25.7 %
Contract brewing and other beer related	2,542	450	2,092	N/M
Alternating proprietorship	9,846	10,744	(898)	(8.4)%
Gross sales	140,852	133,308	7,544	5.7 %
Excise taxes	(9,121)	(8,595)	(526)	6.1 %
Net sales	$ 131,731	$ 124,713	$ 7,018	5.6 %

(1) Other sales include sales of promotional merchandise and other.

N/M – Not meaningful

Shipments by Category

Shipments by category were as follows (in barrels):

Year Ended December 31,	2011 Shipments	2010 Shipments	Increase	% Change	Change in Depletions(1)
A-B	611,200	574,900	36,300	6.3 %	6.5 %
Contract brewing	49,300	23,100	26,200	113.4 %	
Pubs and Other	12,100	9,800	2,300	23.5 %	
Total	672,600	607,800	64,800	10.7 %	

Year Ended December 31,	2010 Shipments	2009 Shipments	Increase	% Change	Change in Depletions(1)
A-B	574,900	573,200	1,700	0.3 %	1.6 %
Contract brewing	23,100	5,000	18,100	362.0 %	
Pubs and Other	9,800	9,300	500	5.4 %	
Total	607,800	587,500	20,300	3.5 %	

(1) Change in depletions reflects the year-over-year change in barrel volume sales of beer by wholesalers to retailers.

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Shipments by Brand

The following table sets forth a comparison of shipments by brand (in barrels):

Year Ended December 31,	2011 Shipments	2010 Shipments	Increase (Decrease)	% Change	Change in Depletions
Widmer Brothers	271,200	277,200	(6,000)	(2.2)%	(2.1)%
Redhook	179,300	174,100	5,200	3.0%	3.0%
Kona	172,800	133,400	39,400	29.5%	29.0%
Total(1)	623,300	584,700	38,600	6.6%	6.5%

Year Ended December 31,	2010 Shipments	2009 Shipments	Increase (Decrease)	% Change	Change in Depletions
Widmer Brothers	277,200	285,700	(8,500)	(3.0)%	(2.0)%
Redhook	174,100	183,600	(9,500)	(5.2)%	(3.3)%
Kona	133,400	113,200	20,200	17.8%	18.5%
Total(1)	584,700	582,500	2,200	0.4%	1.6%

(1) Total shipments by brand exclude private label shipments produced under our contract brewing arrangements.

The 6.6% increase in total shipments in 2011 compared to 2010 was primarily driven by our increased sales and marketing efforts and new brand and package introductions, which began in the fourth quarter of 2010. The rate of change in depletions, or sales by the wholesalers to retailers, for the Widmer Brothers, Redhook, and Kona beers increased 6.5% compared to 2010.

The increase in sales dollars to A-B and A-B related in 2011 compared to 2010 was primarily due to an increase in volume, higher selling prices for our beers and a shift in product mix towards bottle and high-end product, both of which carry a higher price per unit than draft. Gross sales were also favorably impacted by a decrease in the per barrel fee associated with sales to A-B as a result of amendments to our A-B Distributor Agreement, which is netted against revenue. Our savings from both the 2010 and 2011 amendments to the A-B Distributor Agreement approximated $3.9 for 2011. The amount of increase in sales realized for future periods may differ from these estimates due to the level, timing and geographic distribution of our shipments to A-B.

Exclusive of the impact of the favorable change in our per barrel margin fee, the average revenue per barrel on shipments of beer through the A-B distribution network increased by 4.4% in 2011 compared to 2010 and 2.8% in 2010 compared to 2009, primarily due to pricing increases and a shift in product mix towards both bottle and high-end product as mentioned above. Price changes implemented by us have generally followed craft beer market pricing trends. During 2011, 2010 and 2009, we sold 90.9%, 94.6% and 97.6%, respectively, of our beer through A-B at wholesale pricing levels.

The following table sets forth a comparison of our shipments by package, excluding private label shipments produced under our contract brewing arrangements (in barrels):

Year Ended	2011		2010		2009	
December 31,	Shipments	% of Total	Shipments	% of Total	Shipments	% of Total
Draft	219,400	35.2%	227,100	38.8%	236,500	40.6%
Bottle	403,900	64.8%	357,600	61.2%	346,000	59.4%
Total	623,300	100.0%	584,700	100.0%	582,500	100.0%

The decrease in the Widmer Brothers brand shipments was primarily due to the continuing pressure on our Hefeweizen beer in the very competitive wheat beer category in the craft segment. This increased competition from large, multi-national wheat beer competitors had a negative impact on Hefeweizen sales. Partially offsetting this decrease was the success of our focus on the Core and High-End Widmer Brothers brands, which is fueling broader awareness of the overall Widmer Brothers brand.

We believe the growth in our Redhook brand during 2011 was a result of our investments in new packaging, brand introductions, and marketing initiatives.

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Kona continues to be one of the fastest growing brands in the craft category, as seen in the increase in shipments in 2011 compared to 2010 and 2010 compared to 2009. This is based on the consumer's connection with the Always Aloha message and quality of the beer.

The increase in contract brewing sales in 2011 compared to 2010 was primarily due to an increase in shipments under an existing third-party contract and the contribution of shipments under a new three-year contract brewing arrangement with FSB, which was entered into in the first quarter of 2011.

The increase in Pubs and Other sales in 2011 compared to 2010 was primarily due to the addition of pub operations acquired with the KBC Merger.

The increase in contract brewing sales in 2010 compared to 2009 was due to a full year of shipments in 2010 compared to roughly one quarter of shipments in 2009.

Prior to the KBC Merger, we earned revenue in connection with an alternating proprietorship agreement with Kona, including fees for leasing the Oregon Brewery and sales of raw materials. Subsequent to the KBC Merger, any such intercompany activities are eliminated, including the revenues associated with the alternating proprietorship agreement.

The increase in excise taxes in 2011 compared to 2010 was driven by three factors: i) increases in shipments; ii) the addition of excise taxes relating to shipments of Kona beers that were previously recognized by Kona prior to the KBC Merger; and iii) a marginal tax rate increase after the KBC Merger as the combined companies are eligible for only a single excise tax exemption. Increase in shipment volume was the most significant factor for the increase in excise taxes in 2010 compared to 2009. Also contributing to the increases in both periods was an increase in the marginal tax rate for beer produced in Washington state, which became effective in the second half of 2010.

Cost of Sales

Cost of sales includes purchased raw materials, direct labor, overhead and shipping costs.

Information regarding cost of sales was as follows (dollars in thousands):

	Year Ended December 31, 2011	2010	Dollar Change	% Change
Beer Related	$ 84,159	$ 85,956	$ (1,797)	(2.1)%
Pubs and Other	19,852	12,108	7,744	64.0 %
Total	$ 104,011	$ 98,064	$ 5,947	6.1 %

	2010	2009		
Beer Related	$ 85,956	$ 87,612	$ (1,656)	(1.9)%
Pubs and Other	12,108	9,618	2,490	25.9 %
Total	$ 98,064			