

Trends in global spirits production

The shaky global economy of the last three years and the growing dominance of the emerging economies have been the main drivers of change in the global distilled spirits industry.

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Economic uncertainties have affected consumer choice on alcohol beverage spending and created a trading down to value brand options and declines in on-premise sales.

This year, even while high unemployment and the downgrading of government credit ratings has consumers questioning the future direction of the fragile economy, consumers are slowly returning to premiumisation in their spirits choices. On-trade growth is slowly climbing and the global spirits market continues to grow, albeit at a slower rate than prior to the recession.

Emerging markets were evidently less affected by recession and have rebounded more quickly than many developed markets. While fighting their own challenges of high inflation, the emerging economies are growing faster than developed economies and are proving to be the key engine for global spirits growth. Analysis company Euromonitor predicts that China alone will contribute 50% of the total absolute volume growth of the spirits industry in coming years.

The evolving global landscape

China is the largest global spirits market. China and India are the two fastest-growing markets for spirits. India is expected to overtake Russia as the second largest spirits market by 2013. In China, the traditional domestic white spirit, Baijiu dominates its \$41 bn alcohol beverage market in both volume and revenue terms. With more than 4 bn litres of these largely sorghum-based spirits sold in China last year, Euromonitor predicts that sales will increase by another billion over the next five years. As is seen in other emerging markets, China is home to many thousands of distillers and a vast number of local brands.

However, while baijiu represents a large majority of the spirits consumed in China, the largest selling brands are not baijius, but rather, the imported Chivas Regal, Hennessy and Johnnie Walker. While outselling every brand of baijiu, less than 2.5 million cases of these leading brands collectively were sold in China last year.

While the Chinese market continues to



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grow in size and value, it also continues to catch the interest of global multinational spirits companies. This was highlighted in July by Diageo's acquisition of baijiu maker Shui Jing Fang, which Diageo hopes to develop into a global brand. Diageo is making it very clear that they are shifting focus and shifting investment from the mature markets of Europe and North America to the faster-growing emerging markets planning for half of its sales to come from developing economies within the next four years. India has rocketed to a position of high significance in the global spirits scene in recent years. India's economy grew at a 7.8% annual growth rate in the first quarter of 2011, and this booming market continues to grow in importance to the global spirits players. India is currently the fifth-largest market for Pernod-Ricard, but it has been stated that it may rank among its top three markets in five years.

This year India's United Spirits Ltd. became the world's largest volume producer of distilled beverages. With a CAGR of 14%, it outpaces all multinational companies. At home, United Spirits produces the countries' top three selling spirits brands, each of them an Indian whisky. United Spirits has a dominant sector position, with a 59% share of the Indian spirits market and it owns 20 brands with million-plus annual case volumes. Indian whisky is primarily molasses-based and this creates reluctance for some whisky producers to accept the Indian spirits as whiskies. Nevertheless, the Indian whisky category is large, it is successful and it is growing with great strength.

The United States is predicted to be the third fastest-growing spirits market through 2015. The US market has shown a gradual recovery in 2010 and 2011, with spirits volume up 2% in 2010 and a steady return to premium spirits. Vodka showed a strong



Alembic stills being used in the production of Cachaça in Brazil.

growth rate of 6.1% in 2010. Whisk(e)y volumes showed 1.4% volume growth, but Irish and Single Malt Scotch, as well as Super Premium domestic and imported whiskies showed strong double-digit growth. Tequila volume grew 3.6% last year, continuing the steady growth that tequila has shown in the US in the last decade. Tequila sales in the US have grown 47% since 2003, with strongest growth in premium priced and 100% agave tequila styles.

Craft distilling is a growing phenomenon in the US (and in Canada to a lesser extent), and the number of licensed craft distilleries has grown from 69 to 240 since 2003. It is

projected that there will be as many as 450 licensed craft distillers in the US and Canada by the end of 2015. The craft movement is generating strong interest in new expressions of American whiskies, brandies, gins and infused vodkas, and the market is seeing the larger distillers take notice of this renaissance in north American spirits.

Spirits categories trends

Vodka

Considered the world's largest spirits category, vodka finds its largest markets in Russia and the United States. Vodka is produced in many countries using ingredients

and production methods dictated by the country of origin. Strong vodka growth in the US and emerging countries such as India are expected to keep vodka in the number one position in the coming years.

Soju and Shochu

These traditional products of Korea and Japan represent the second largest spirits category. They are consumed mostly in their home countries, while Japan also imports large volumes of Soju. The world's largest selling distilled spirits brand is the Soju brand; Jinro. Soju is a colourless spirit produced from a wide variety of materials, including sorghum, rice, tapioca, barley and other grains. Japanese Shochu is more commonly produced from rice. A unique 'solid-state' fermentation process call *Koji* fermentation is used in the production of traditional styles of Shochu. The *Koji* process utilises specific strains of fungi, which are grown on steam-softened grains to allow for conversion of the grain starches into fermentable sugars before the grains are sent to fermentation. This can produce special spirits that are highly valued.

Cachaça

Brazil produces more than 1.3 billion litres of cachaça annually by some 30-40,000 small and medium size distillers. Produced from fresh-pressed cane juice, cachaça can only be produced during the cane harvest season. Less than 1% of cachaça is currently exported. Export markets are key to the growth of this spirit style, which has shown flat volumes in recent years. Some 160 cachaça producers export to 60 countries, with Germany providing the largest market, followed by the US. Producers are looking to attract greater export opportunities by upscaling their products. Barrel ageing in reused bourbon casks and in vats from Brazilian woods, along with better control of quality consistency, are creating cachaças of higher image that are better positioned to appeal to the lucrative foreign markets.

Whisky

In the UK between 2005 and 2009, the value of Scotch consumption in the home market dropped 23% as it continued to lose volume to vodka and other spirits types. Reports have compared the global growth in Scotch whisky volumes against vodka growth and the results have cast a sobering light on Scotch. Data shows that vodka volumes grew at more than five-times the rate of Scotch growth during a 20 year period from 1998 to 2008. I am not sure that this is a fair comparison and perhaps it is fairer to compare Scotch whisky growth against non-Scotch whiskies.

Whiskies of all types showed a sharp decline in volume in the late 1980s and the decline lasted as long as ten years. During the next decade, Scotch whisky showed ups and downs in volume sales, displaying record-setting growth in 2006 followed by flat overall growth in 2007. Declines in the once-



Large scale fermentation at a Canadian whiskey distillery.

dominant Scotch markets of France and Spain were balanced by strong growth in emerging markets in those years. Again in 2010 Scotch exports surged to a new record of £3.45bn. Similarly, malt whiskies also showed volume growth in 2006 (23%) and now, post-recession, is again showing strong growth. Performance of the predominant non-Scotch whiskies; namely Canadian, American, Irish, Japanese and Indian, has been varied in recent years. Canadian whisky sales have remained fairly flat, while American whiskey experienced 2% CAGR between 2003 and 2008. Irish whiskey has been one of the fastest growing spirits categories in recent years, thanks in large part to very strong growth in the US. Indian whisky, while not impacting much on global markets, is showing double digit growth within India.

Other spirits trends

- Cognac sales declined sharply in the 1990s but made up all lost volume by 2007. The recession took its toll on cognac sales but 2010 saw record growth, with a 17.9% volume increase and nearly 30% value growth in one year.
- Increased marketing spend in rum, along with premiumisation and innovation, is upscaling the image of rum and driving increased sales. Sustained growth is coming from continued cocktail popularity and growth in flavoured spirits.
- International Wine & Spirit Research (IWSR) is predicting a 2.5% drop in gin sales in its five-year spirits forecast (2010-2014)
- Vodka remains the spirit of choice of the Russian people. Vodka is produced by a large number of distillers, and the top three brands provide less than 8% of the total spirits consumed in Russia.

Brand trends

Smirnoff vodka took the top spot in a report by IWSR listing the best selling 'international spirits brands' in 2010/2011. Bacardi rum and Johnnie Walker Scotch whisky placed second and third, while Green Mark Russian vodka edged out Absolut vodka for fourth largest selling international brand. In comparing 2009-2010 volume growth, the same report showed Johnnie Walker as the largest growing 'international' brand, with Absolut and Smirnoff placing second and third. The IWSR considers international brands to be those demonstrating sales of over 20,000 cases in at least three geographic regions, including travel retail as one region. Another new IWSR report ranks the top 100 volume spirits brands in the world and shows a very Asia-dominated view of the spirits world. Here the familiar international brands sit lower in the overall standings.

The report shows that forty-six of the world's 100 largest brands are from the Asia-Pacific region. South Korean Jinro Soju is the undisputed global spirits brand, with more than double the sales volume of second-place

Top ten International* spirit brands from IWSR

Rank 2010	Rank 2011	Brand	Category	'000s 9-litre cases
1	1	Smirnoff Vodka	Vodka	24414
2	2	Bacardi Rum	Rum	18749
3	3	Johnnie Walker	Whisk(e)y	15543
-	4	Green Mark Vodka	Vodka	11191
4	5	Absolut	Vodka	11004
5	6	Jack Daniels	Whisk(e)y	10148
6	7	Nemiroff	Vodka	9119
7	8	Captain Morgan Rum	Rum	8898
-	9	Khlibniy Dar	Vodka	8129
8	10	Baileys	Flavoured	6604

*Selling more than 20,000 cases across at least three regions

The real top ten from IWSR showing the top three international spirits swamped by local brands

Rank 2010	Brand	Category	'000 cases
1	Jinro - Korea	Soju	67655
2	Ruang Kao - Thailand	Others	30000
3	Smirnoff	Vodka	24414
4	Cachaca 51 - Brazil	Cane	19478
5	Bacardi	Rum	18749
6	San Miguel - Philippines	Gin	18650
7	Bagpiper - India	Whisk(e)y	16926
8	Kyongwal - Korea	Soju	15676
9	Johnnie Walker	Whisk(e)y	15543
10	McDowells - India	Whisk(e)y	15377

Ruang Kao, a rum-like spirit from Thailand. The list is dominated by vodka and Soju/Shochu, and shows Smirnoff vodka in third place and Absolut placing 19th. Seventeen brands of whisky made the top 100 list, with 15 of the brands hailing from India. This highlights the impressive strength of the spirits brands in the emerging Asian markets. In this definitive list, Bacardi stands as the fifth largest brand and Johnnie Walker is placed in 9th spot.

Another dramatic view of the global market is shown by IWSR's ranking of the top 25 fastest growing (2009-2010) spirits brands. The top five fastest growing brands are Indian, which are sold almost exclusively in their domestic market. Eight of the top 25 are Indian whiskies and the fastest growing 'international' spirit; Johnnie Walker Scotch whisky, sits in 14th position.

Future trends

Consumer need-states drive consumer choices. Consumers will continue to demand more distilled spirits choices, and this will be driven by needs around active lifestyles, healthy living, high quality and product convenience. Consumers today also have a strong desire for new experiences. This should lead to continued growth in the variety and diversity of new spirits types. I can see continuing growth in products containing healthy ingredients; antioxidants, teas and fruit juices, and I see a small but rising interest in organic spirits.

Consumers will continue to trade up to premium products so long as the economy

continues to strengthen.

I do not see strong support in the developed Western markets for baijiu and I predict slow export growth for cachaça. I believe that stricter standards of definition are needed for cachaça, at least for export markets, to help narrow the large range of taste styles in the category, to enable the consumer to better identify a common taste thread for cachaça.

A new product must become familiar to the consumer before acceptance is gained.

I see opportunity for strong growth of non-Scotch whiskies, which, because of their more mixable styles, will continue to benefit from the strong consumer interest in cocktails. Flavoured whiskies and whisky RTDs will also drive new growth.

Women are gaining more attention from spirits marketers, and are becoming the prime targets for new product development, especially for new flavoured spirits. Flavoured vodkas and rums make up the majority of new product launches and will continue to attract new consumers to the spirits market.

China and India are expected to remain the fastest-growing spirits markets in coming years, and the global spirits market is expected to continue growing, but at a slower rate than recent years. Multi-national companies will continue to build exposure to these emerging markets. Industry consolidation will also continue into the future. Spirits companies are not yet as consolidated as the brewers, and the continued movement toward emerging market exposure will likely expose ideal opportunities for acquisitions. ■