



THE DRINKS MARKET

PERFORMANCE IN 2009

PREPARED FOR

Drinks Industry Group of Ireland

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Contents

Section	Title
1	Overview of 2009 Market
2	Introduction and Economic Environment
3	Volume of Alcohol Consumption
4	Product Mix
5	Prices
6	Budget 2010 and Alcohol Taxation
7	Retail Sales in Bars
8	Off Licence Performance
9	Value of Sales
10	2010 Prospects

1. Overview of 2009 Market

- In last year's Drinks Market Performance 2008 was described as the worst performance in decades for the overall drinks industry. Unfortunately the 2009 performance was worse than 2008 and the title of worst year now passes to 2009. The poor drinks performance was driven mainly by the historically weak national economic situation. GDP volume declined by 7.5% in 2009, GNP volume declined by 10.4% and the volume of total national consumer expenditure declined by 7.2 %. National employment decreased by 7.8%. In addition, cross border purchases continued to be attractive, driven by the exchange rate and excise and VAT differentials.
- The 2008 Drinks Market Performance predicted a decline of about 10% in the 2009 total alcohol volume and, unfortunately, this has largely been realised.
- The volume of total alcohol consumption as measured by Revenue clearances declined by 8.9% in 2009. This follows a decline of 5.9% in 2008. Even when the increased level of cross border sales is allowed for there is still a substantial consumption decline of over 7% in 2009.
- The volume of alcohol consumption as measured by Revenue clearances is now just over 40M LPA and is back to the level of 1999.
- Per adult consumption decreased by 9.2% in 2009 following a 7.3% decline in 2008.
- Per capita consumption decreased by 9.6% in 2009 following a decline of 7.7% in 2008.
- Average alcohol consumption in 2009 is back at the 1995/96 level.
- All four alcohol drinks categories, beer, spirits, cider and wine had volume declines but spirits were hit the hardest. The lowest decline was cider at 5.9%.

Beer declined in volume terms by 6.5%. Wine declined by 6.9%. Spirits declined by 18.5%.

- The individual product market volume shares in 2009 were wine 23.3%, beer 50.7%, spirits 17.5% and cider 8.5%.
- Soft drinks consumption volume declined by 7.1% in 2009 and bottled water volume declined by a very large 19.5%.
- Alcohol excise receipts declined by 10% in 2009.
- Between Jan and Dec of 2009 on licence prices declined by 0.3%. off licence prices declined by 4.8% and total alcohol prices declined by 1.6%.
- On licence alcohol prices were 2.3% higher on average in 2009 compared to 2008. However, this increase was due to the carryover effect of the October/November/December 2008 price increases caused by the increase in wine excise, the VAT increase from 21% to 21.5% and a price increase by some suppliers.
- Off licence prices rose by 2.2% in 2009 compared with 2008. Alcohol prices as a whole increased by 2.3%.
- On licence prices decreased by 2.7% in January 2010 compared to December due to the excise and VAT reductions in the December budget
- The value of the alcohol market declined by 6.8% to €6.55Billion.
- Bar sales volume, which includes food sales, soft drinks and off licence as well as bar sales of alcohol, decreased by 11.1% in 2009 following the 2008 decline of 6.8%. The value of sales decreased by 8.8% in 2009. The volume of bar sales

of alcohol declined by about 12% in 2009 and there was an estimated 6% decline in off licence sales volume.

- Prospects for the Irish drinks market in 2010 remain very weak. GDP is currently forecast by Government to decline by 1.3% in 2009. While the consensus is for further declines in economic activity in 2010 one private forecaster is expecting a slight increase. The volume of consumer expenditure will decline by 3.0% according to Government forecasts. The higher level of tax, increased mortgage rates and pay cuts and pay freezes will reduce discretionary income. The factors, in particular the tax gap, encouraging cross border shopping have reduced, although there is still a tax based financial incentive to do so for spirits and wine . One would hope to see a stabilisation and possible reduction in the scale of cross border alcohol purchases.
- Despite the welcome reduction in VAT in the December 2009 budget the level of alcohol taxation in Ireland remains very high by EU standards. Spirits excise in the Republic of Ireland is still 24.7% greater than Northern Ireland.
- Based on the expected economic decline the alcohol market will continue to decline in 2010. Total alcohol volume could decline by 5% but with a larger decline of 7% in the employment intensive on licensed sector.

2. Introduction and Weak Economic Environment

This report examines the performance of the alcohol and soft drinks market in 2009. It deals with total and per capita consumption, product mix, prices, value and volume of sales and the distribution between on and off-licence sales.

The report is mainly based on official data sources from the Revenue Commissioners and the Central Statistics Office and is compiled by Anthony Foley, Dublin City University Business School. The emphasis on official data sources is designed to facilitate external scrutiny of the analysis. In some limited cases there is use of industry market research data where official data are unavailable.

The drinks market performance was very weak in 2009, which followed the weak performance in 2008. This was driven by the poor national economic performance. Real GDP declined by 7.5% in 2009. Real GNP declined by 10.4%. Real consumer expenditure declined by 7.2%. National employment declined by 7.8% and the average unemployment rate was 11.8%. Income tax increases and pay cuts reduced disposable income. The alcohol tax differential with Northern Ireland and the exchange rate continued to make cross border purchasing of alcohol attractive in 2009. Given the overall decline in economic activity and the very weak economic environment it is not surprising that the drinks market declined substantially and by unprecedented levels in 2009.

3. Volume of Alcohol Consumption

The most generally used domestic and international indicator of aggregate alcohol consumption is quantity of pure alcohol contained in the various beverages. In calculating the aggregate alcohol volume wine was based on a 12.5% alcohol content and cider was based on a 5% alcohol content. Based on Revenue Commissioners data for the four beverages groups, the volume of alcohol decreased by 8.9% in 2009 compared with 2008. This follows the 2008 decline of 5.9%. Some industry market research data indicates a larger decline in consumption (11%) than the Revenue clearances data decline of almost 9%. Excise receipts from alcohol declined by 10% in 2009. The 2009 total alcohol volume of 40M LPA has fallen back to the level of 1999.

On a per capita basis there was a decrease of 9.6% from 9.937 litres of pure alcohol in 2008 to 8.979 litres in 2009. Per adult consumption declined by 9.2% from 12.520 litres of pure alcohol in 2008 to 11.370 litres of pure alcohol in 2009. The 2009 reduction has brought alcohol average consumption back to the 1995/96 levels and well below the peak average consumption levels of 2001. Per capita consumption in 2009 is 20.8% below the peak 2001 level. The 2009 per adult consumption is 21.3% below the peak level of 2001.

Table 1 Volume of Alcohol Consumption 2008 and 2009

	1995/96 Average consumption	Peak average consumption 2001	2008	2009	% change (08/09)
Total Volume (MLPA)	Not applicable	Not applicable	43.948	40.042	-8.9
Per capita(LPA)	9.20(1996)	11.33	9.937	8.979	-9.6
Per adult(LPA)	11.35(1995) 12.06(1996)	14.44	12.520	11.370	-9.2

Source: Derived from Revenue Commissioners and CSO.

In the face of continuing, albeit low, population growth in 2009 (+0.8%) the large volume decline was driven by substantially reduced average consumption per person and per adult.

The Revenue clearances measure has a number of shortcomings as an indicator of national domestic consumption. It does not allow for out of state sourcing such as cross border purchases, it does not allow for changes in stocks of retailers and it does not allow for the quantities consumed by visitors to Ireland. The most immediate of these issues is the growth in cross border purchases. Between 2008 and 2009 the increase in cross border consumption may have been the equivalent of about 3% of the Republic's off licence trade which equates to about 1.5% of total consumption in the Republic. Consequently, while the Revenue data indicate a clearances/consumption decline of 8.9% the likely actual consumption decline is about 7.4%.

4. Product Mix

The official Revenue data divides alcohol into beer, cider, wine and spirits. All four categories experienced declines. The lowest decline in 2009 was cider. The volume of cider consumption decreased by 5.9%. Beer volume declined by 6.5%. The wine volume change was a decrease of 6.9% and the spirits decrease was 18.5%.

The consumption shares of the four product categories in 2009 were beer 50.7%, spirits 17.5%, wine 23.3% and cider 8.5%.

Table 2 Product Category Mix and Growth 2008 and 2009

	Beer	Spirits	Wine	Cider
% Share 2008	49.4	19.5	22.8	8.2
% Share 2009	50.7	17.5	23.3	8.5
% Increase in volume 2008/09	-6.5	-18.5	-6.9	-5.9

Source: Revenue Commissioners

The soft drinks volume declined by 7.1% in 2009. The bottled water volume decline was very large at 19.5%.

5. Prices

Within 2009 alcohol prices declined. Between January and Dec of 2009 on licence prices declined by 0.3%, off licence prices declined by 4.8% and total alcohol prices declined by 1.6%.

The price performances of the two drinks sectors in 2009 are shown in Table 3.

Table 3 Price Changes (%), on and off licence sectors within 2009, Jan to Dec

	On licence	Off licence	Total Alcohol
% change between Jan and Dec 2009	-0.3	-4.8	-1.6

Source: CSO

Following the excise reduction in December on licence prices declined by 2.7% in January 2010 compared with December. Off licence prices declined by 1.4% in January following an earlier decline of 3.4% in December. The overall alcohol price declined by 1.6% in January. Alcohol prices declined by an additional 0.5% in February compared with January.

As measured by the Consumer Price Index (CPI) average alcohol prices in 2009 were 2.3% higher than in 2008. This compares with an overall CPI decrease of 4.5%. However, the CPI excluding mortgage interest declined by only 1.2%. On licence prices increased by 2.3% and off licence prices increased by 2.2%.

Table 4 Alcohol Price Change 2009 compared with 2008

	% change
All Alcoholic Drink	2.3
Off Licence	2.2
On Licence	2.3
CPI	- 4.5
CPI excluding mortgage interest	-1.2

SourceL: Derived from CPI CSO.

The price changes referred to above are average prices in 2009 compared with average prices in 2008. Consequently they give an inaccurate picture of price changes within 2009 as already identified in Table 3. Several factors caused the alcohol price to increase in October/November/December of 2008 including the VAT increase from 21% to 21.5%, the increase in wine excise of 50 cent per standard bottle and a price increase by some suppliers. The carryover effect of this into 2009 is the cause of the average 2009 on licence price increase compared to 2008.

6. Budget 2010 and Alcohol Taxation

Budget 2010 reduced alcohol excise by approximately 20% and also reduced the VAT rate from 21.5% to 21%. This will be a very welcome boost to the drinks market in 2010. The impact of these reductions have been seen in the alcohol price reductions in January. Taken together with the VAT increase from 15% to 17.5% in Northern Ireland the excise reductions have lowered the incentive for cross border purchasing but they do not remove the fiscal incentives. The Republic's spirits excise is 24.7% higher than the UK and the wine excise is 11.1% higher. Beer excise in the Republic is now lower than in the North but the main driver of cross border purchasing is spirits. In addition the Republic's VAT is 21% compared to 17.5% in the North.

Despite the very welcome alcohol excise decreases in the December budget Irish alcohol taxation remains high by EU standards. In 2010 Ireland has the third highest spirits tax after Sweden and Finland, the second highest wine excise after Finland and the fourth highest beer tax after Finland, the UK and Sweden. This will continue to have negative effects on tourism competitiveness at a time when it is essential to support economic activity to the greatest extent possible.

7. Retail Sales in Bars

Total alcohol consumption, which includes both on and off licence sales declined by 8.9% in 2009 when measured by Revenue clearances data. The volume of bar sales decreased by 11.1% in 2009 according to the CSO and the value declined by 8.8%. The bar sales index covers all bar sales including food, soft drinks and off licence sales as well as bar sales of alcohol. The industry view is that food sales performed better than drinks sales. This was also the pattern in 2008. Consequently, the decline in drinks sales in bars was larger than the overall Retail Sales Index figure compiled by the CSO. Based on industry and market research information it is estimated that the volume decline in alcohol sales in bars was approximately 12% in 2009.

Table 5 Bar Sales % Change

	Volume	Value
2008/09	-11.1	-8.8

Source: CSO

8. Off Licence Performance

The off licence share of alcohol consumption has increased over the medium term. Based on sales within the Republic of Ireland the 2009 volume shares were estimated to be approximately 50% on licence and 50% off licence. However, a portion of home consumption is sourced from Northern Ireland. When this is included more than 50% of alcohol consumption is home consumption. Official comprehensive data on off licence volumes are not available but it is possible to make a reasonable estimate using the Revenue data and the Index of Retail Sales.

The off licence sales volume is estimated to have declined by 6% based on the official figures for overall clearances and bar retail sales. Excluding the impact of cross border off licence sales the off licence share of total alcohol consumption in 2009 was 49% compared to 47% in 2008. The inclusion of cross border sourced off licence sales increases the off licence share to 51%.

9. Value of Sales

The volume decrease was 8.9% in 2009 compared with 2008 and there was a value decrease of 6.8%. The 2008 CSO estimate of alcohol personal expenditure was €7.028B in 2008. This suggests an expenditure level in 2009 of €6.55B.

Table 6 Value and Volume Changes in the Alcohol Market 2009

	%
Volume change	-8.9
Value change	-6.8
Value Estimate 2009	€6.55B

Source: Revenue Commissioners and CSO

10. 2010 Prospects

The consensus in economic forecasts is that the Irish economy will decline further in 2010 but at a much lower rate than in 2009. The decline in GDP/GNP will be concentrated in the first half of the year and by the third and fourth quarters modest economic growth will be resumed. One private forecaster is predicting an increase in economic activity in 2010. While the annual GDP and GNP declines will be substantially lower in 2010 than in 2009 the relative improvement in total consumer expenditure will be less notable. Further decline in the drinks industry can be expected in 2010. The euro will continue to be strong relative to Sterling. The alcohol tax differential with the North has improved because of the excise reduction in the December 2009 Budget and the increase in the UK VAT rate. However, there is still an incentive to source from over the border for spirits and wine which could be enhanced by the pressure on incomes and the search for economies by consumers.

On licence prices declined in January 2010 due to the excise reduction in December which will assist bar sales volume but will have a negative effect on value of sales.. There will be substantial pressure on personal disposable incomes and discretionary incomes due to the new higher income tax rates, unemployment and pay cuts and pay freezes and likely interest rate increases.

According to the Government forecasts as of December 2009 the GNP performance will improve from a decline of 10.4% in 2009 to a decline of 1.7% in 2010 and GDP will improve from a decline of 7.5% in 2009 to a decline of 1.3% in 2010. Unfortunately, total consumer expenditure which is a significant determinant of alcohol volumes will improve by less from a decline of 7.2% in 2009 to a decline of 3.0% in 2010.

The recent (January) Central Bank forecast includes an expectation that total consumer volume will decline by 3% in 2010. The January AIB forecast expects a total consumer decline of 3.5% in 2010. The March IBEC forecast is more optimistic than it's previous forecast but a decline of 2.5 % in total consumer volume is expected. The most recent ESRI forecast of winter 2009 expected a 1% decline in consumer

expenditure while the September Davy forecast included an expectation of an increase of 1.5% in the 2010 volume of consumer expenditure.

The forecast 3% decline in the volume of overall consumer expenditure in 2010 will have a substantial negative impact on alcohol consumption volume which will be mitigated to a small degree by the improvement in cross border competitiveness and the reduction in alcohol prices. One welcome sign is the January 2010 Retail Sales Index which reported an increase of 0.2% in the volume of bar sales on a seasonally adjusted basis. However, it should be noted that bar volume increased between December 08 and January 09 but the eventual overall 2009 performance was a large decline in volume.

The national consumer expenditure performance is determined by disposable income, the wealth effect and confidence. It will not be possible to improve the first two determinants in 2010. Any improvement in consumption will come about from increased consumer confidence and a reduction in the savings rate. Confidence will be determined mainly by progress on NAMA/banks and the correction of the public finances and also by the international recovery. If no major new negatives emerge on the NAMA/banking and public financial correction fronts the decline in national consumption will be about 2.5%. Unexpected good news on these two fronts would improve confidence and generate a better than expected consumption performance. Unfortunately, the reverse could also occur, bad news on these two fronts will weaken consumer confidence.

A continuation of the 2009 link between alcohol volume decline and overall consumer expenditure where alcohol volume declined by almost 9% compared to a consumer expenditure volume decline of 7.2% would imply that the expected 2.5% consumer expenditure decline would be associated with an alcohol decline of 3.5% excluding any benefits from reduced cross border shopping. However, in 2009, the alcohol decline was much closer to the overall consumer expenditure decline than in previous years. In the 2004 to 2008 period alcohol volume underperformed total consumer expenditure by an average of 3.5 to 4 percentage points depending on the

alcohol volume indicator used. Apart from the impact of the recession the industry is affected by the medium term decline in average consumption and the ongoing shift to home consumption. The 2010 forecast is based on the medium term alcohol to total consumer expenditure pattern. It assumes some improvement in cross border purchasing and no alcohol price increases.

Based on current economic expectations, including a total consumer expenditure volume decline of 2.5%, alcohol volume could decline by 5% in 2010 with a larger decline of 7% in the employment intensive on licence sector.