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THE “PREMIUMISATION” OF WHITE SPIRITS

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INTRODUCTION

The global white spirits market is complex and vast. There is a plethora of brands, categories, quality levels, international and local spirits. In order to get any meaningful overview, it is necessary to break the market down into individual categories.

VODKA

Vodka is the world’s best selling spirit but posted a 1% total volume decline in 2009 amounting to 415 million cases.¹ However, it was the fall of 3% in volume sales in Eastern European markets that depressed these figures. Eastern Europe still accounts for 67% of global volumes so any weakness in this market will skew the figures. Conversely, total volume sales grew by 7% in Asia-Pacific, 8% in Australasia, 4% in the Middle East and Africa, 3% in North America and 4% in Western Europe.²

The global market for Vodka above the US$8-9 level is 100 million cases worth $36 billion annually with Smirnoff accounting for 25% of this market. Cheap “$1-a-bottle-stuff” in Russia, Eastern Europe and Asia accounts for a further 300 million cases.³

The US has almost 60% of the global premium vodka market⁴ and some 30% of total industry volume.⁵

The UK market is likely to nudge over £2 billion (11 million cases) with total sales rising by 20% over the last 5 years and premium sales up 40%.⁶

Asia and particularly India are experiencing large growth. India almost doubled growth in the last 5 years to 58 million cases and the Asia Pacific region is expecting 8% CAGR for the next 5 years.⁷

The global vodka market is one of the most fragmented of all spirit categories with the top five producers accounting for only 22% of global sales despite Smirnoff’s dominance in Western markets.⁸

GIN

Global gin sales, which add up to approximately 50 million cases by volume⁹, have declined slightly in recent years. This small weakening in the overall figure hides the growth in the premium sector which continues to grow in the order of 2.5% annually¹⁰. Spain is Europe’s leading gin consumer, the majority being domestic brands accounting for 75% of sales¹¹, but has suffered a fall of 7% in volume. India on the other hand, which has been increasing its premium market with the rise in numbers of an affluent middle class, has reported a 7% rise in volume.

¹ Drinks International March 2010
² Drinks International March 2010
³ Drinks International Nov/Dec 2009
⁴ Drinks International March 2010
⁵ Spirits Business Vodka Yearbook 2010
⁷ Drinks International March 2010
⁸ Drinks International March 2010
⁹ IWSR
¹⁰ Spirits Business Feb 2010
¹¹ Gin and Vodka association website
The Philippines remains the world’s largest gin market accounting for 43.5% of global consumption with a tiny 2% being imported brands.\textsuperscript{12} San Miguel is the world’s largest gin producer\textsuperscript{13}

Distillers have concentrated on value growth as the category still remains static or in slight decline overall. This has led to further investment in super-premium gins and a number have been released in the last 18 months including Bacardi’s Oxley with a retail price of £50.

**RUM**

Bacardi is the runaway market leader in the white rum category selling almost 20 million cases globally.

The US is the dominant market with sales of 125 million litres in 2009 significantly ahead of Brazil in second place with 30 million litres. The UK market is 20 million litres.\textsuperscript{14}

**TEQUILA**

The tequila market continues to show strength with volume sales tripling between 1995 and 2008 from 104 million to 309 million litres.\textsuperscript{15} The market has been invigorated by improvements in the quality and consistency of tequilas from agave, with a shift towards 100% agave and away from inferior mixto tequilas. In 2007, sales of 100% agave tequilas overtook those of mixto and now command 52% market share. \textsuperscript{16}

The tequila market is worth over $4 billion with US as the most important market outside Mexico. According to the Tequila Regulatory Council, nearly 80% of exports go to the US.

European share of exports is 12% or 17 million litres with Germany taking the largest share at 31%.\textsuperscript{17}

Patron dominates the premium category although Diageo and Pernod Ricard have been heavily marketing their respective brands, Jose Cuervo and Olmeca in an attempt to drive further premiumisation within the category.

**BAIJIU / SHOCHU / SOJU**

The domestic market for these Asian spirits is huge although they are virtually unknown internationally. The South Korean soju market records volume sales of 1 billion litres and the Japanese shochu market is 1.2 billion litres. Jinro dominates the soju market with sales of 64 million cases in 2009 down by nearly 16% with consumers starting to switch to takju (rice wine) after tax breaks were granted by the government.\textsuperscript{18}

The Japanese shochu market is mature and has fewer dominant companies, the largest of which is lichiko at 8.7 million cases, down 4%.

\textsuperscript{12} Gin and Vodka association website
\textsuperscript{13} Gin and Vodka association website
\textsuperscript{14} Drinks Business Dec 2009
\textsuperscript{15} Drinks International Jan 2010
\textsuperscript{16} Drinks International Jan 2010
\textsuperscript{17} Drinks International Jan 2010
\textsuperscript{18} Drinks International July 2010
There are over 18,000 producers of Baijiu in China, in a market that has been growing at 30% annually and currently worth £13.6 billion. The largest producer is Tuopai with sales of 5.5 million cases but only accounting for about 1% of the market illustrating the fragmented nature of the market.

Diageo and Pernod Ricard have forged links with Baijiu producers either by acquisition or local partnerships. Diageo with its stake in Quanxing group has the Sichuan based Swellfun brand and Pernod Ricard with its 51% stake in Jiannanchun Group launched the premium Baijiu Tian Cheng Xiang in 2008.

**CACHACA**

There is a large Brazilian domestic market for cachaca with Pirassununga 51 topping the list with sales of 19.5 million cases in 2009, down 11% although second place brand, Pitu, managed to increase sales by 1%.

**PREMIUMISATION**

Premiumisation began with the introduction of Bombay Sapphire in 1987, gin’s first image driven brand. Bombay Sapphire’s packaging, story and light delicate flavour appealed to the modern drinker brought up on Vodka. Bombay Sapphire started the trend for using exotic botanicals from around the world such as cubeb berries from Java and grains of paradise from West Africa.

The super premium vodka market came to life in the mid 1990s as the category looked for ways to reinvent itself for a new generation of aspirational drinkers. Grey Goose quickly established itself as the market leading vodka, achieving phenomenal growth to over 2.5 million cases by 2005.

According to Andy Fennell, chief marketing officer of Diageo, the generally accepted definition of premium is US$10 and up. $20 and up is super premium and over $30 is ultra premium.

Clearly, the consumer is unwilling to pay a premium for a brand without perceiving that it is somehow superior to a standard bottling. This is where marketing is crucial and the marketers have several weapons at their disposal often using some or all of the following:

- Quality
- Exclusivity
- Unique method of production
- Authenticity
- Ecological or green credentials
- Packaging

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19 Spirits Business Apr 2010
20 Spirits Business Apr 2010
21 Drinks International July 2010
22 WSET Distilling Knowledge pg76
23 Drinks Business Dec 2009
24 Just-drinks interview 27th April 2010
• Celebrity endorsement

QUALITY

Naturally, most producers will claim that their product is of high quality and will emphasize their use of first class and rare ingredients. This is particularly evident in the premium gin sector with its reliance on exotic and enticing botanicals such as Beefeater 24’s use of rare Japanese Sencha tea.

EXCLUSIVITY

A premium can be charged for exclusivity and the idea that the consumer belongs to an elite circle of like minded, successful individuals. Fairfax Hall, co-founder of Sipsmith Gin suggests that the first taste of gin for a new generation of younger drinkers is through premium brands rather than the same old brands they saw their parents drinking. As a result the category has become aspirational and interesting.25

Small batch production also suggests that extra care and attention has gone in to the production of the drink and that artisan methods are being employed. This includes producers such as Hendrick’s and Caorunn.

UNIQUE METHOD OF PRODUCTION

Oxley Gin, a brand owned by Bacardi, has recently launched in the UK and US. This gin uses a unique cold distillation production method where the base spirit is distilled at -5°C in a semi-vacuum. Raquel Faria, Oxley’s worldwide marketing manager, stated that their aim was to “produce a gin that marries authenticity and craftsmanship with innovation and technology.”26

Another example that appeals to the ‘bling’ end of the market is the use of diamonds in the filtration process of Diamond Beverages’ Diamond Standard Polish Vodka.

AUTHENTICITY

Andy Causer, sales director at UB drinks, believes that “provenance is also playing a bigger part in the Vodka market with more originating from outside Russia and Scandinavia. Consumers are actively searching out specific vodkas, of different origins, with a solid heritage behind them.”27 Whilst in the gin market companies such as Beefeater emphasise the fact that their Beefeater 24 London Dry Gin is authentically distilled in London.

Charles Gibb, the head of the Moet Hennessy owned Belvedere brand believes that there has been a significant shift towards brands with authenticity whilst explaining their use of authentic Polish rye.28

25 Drinks Business Nov 2009
26 Just drinks Oxley launch 10th August 2009
27 Drinks Business Oct 2009
28 Vodka Yearbook 2010
ECOLOGICAL CREDENTIALS

Akvinta, a Croatian vodka, uses water from ‘a very ecologically pure source’ and uses organic wheat sourced from the very best producers in Emilia-Romagna.29 IS Vodka meanwhile, blends its vodka with water from an Icelandic glacier claiming that “extraction is managed in an ecologically responsible manner by members of the local Icelandic community.”30

PACKAGING

Some premium products will use their packaging in order to stand out from the competition. The vodka market in particular is congested and it is easy for brands to become lost in the crowd. DQ Vodka, for example has a striking bottle design that is different to anything else currently on the market. DQ co-director Petter Moe says “It is difficult to differentiate a product in such a fierce marketplace, but if you have a product that looks different, is of high quality and you have a brand statement that the customer can identify with, then it is definitely possible to make its presence noticeable.”31

CELEBRITY ENDORSEMENT

Perhaps the clearest demonstration of the power of celebrity endorsement is provided by the partnership between Cîroc, the French Vodka made from grapes, and Sean Coombs, also known as P Diddy. Sales climbed from 60,000 cases in the first half of 2007, when Coombs began his endorsement, to over 400,000 cases in the year ended 30 June 2009.32

More recently Skyy Vodka was the promotional partner and official vodka for the Hollywood blockbuster Sex and the City 2, with its combination of glamour, fashion, sex and cocktails. Andrea Conzonato, COO of Skyy Spirits asserts it is not about product placement but “about creating excitement with distributors, retailers and consumers.” 33

CASE STUDY – CHASE VODKA

Chase distillery is based in Herefordshire and is an English artisan spirits company producing vodka from potatoes grown on the farm owned by Will Chase. Under ever increasing price pressure, Chase felt the need to diversify and in 2002 established Tyrrells making potato chips. While travelling in the US in 2004, he came across a small distillery making vodka from potatoes and decided that he could do the same in the UK. From the idea in 2004, it took until June 2008 to make the first run of vodka.

Initial market research showed ‘it to be full of a lot of ‘twee' marketing stories or large corporate companies’ and that there would be a market if he could make a quality product and sell it with provenance and pedigree.34

29 www.akvinta.com
30 www.isvodka.com
31 Drinks Business Dec 2009
32 Drinks Business Dec 2009
33 Spirits Business May 2010
34 www.chasedistillery.co.uk
Further research, with an eye on ensuring the highest quality, suggested a need for a bespoke rectifying column. The cost of production was always going to be high due to the small volumes produced and the price of the distilling equipment from a German specialist company. This has necessitated positioning the vodka in the super premium price bracket although this was originally Chase’s intention. “Making good vodka wasn’t particularly difficult, mainly because it has been made so badly for so long. But it’s got to be good, or there’s no point doing it. If you start cheap, you’re always cheap,”35

The marketing strategy has therefore focussed on placing the vodka in premium outlets that can afford to sell it and promotion at premium events. According to Caroline Clarke, Chase’s marketing manager, “…for our spirit to be recognised as the world’s best, the marketing model is based around everything that is premium including packaging, marketing material and branding.”36

Chase has promoted its English heritage relying heavily on the idea that it is a locally produced, artisan product using the finest, locally sourced products. “There's a big food and drink revolution at the moment,” says Chase. “What people want to discover is something quite genuine. They want local produce made using traditional methods.”37

Chief distiller Jamie Baxter continues this theme, "We make vodka in a painstakingly traditional fashion. Most vodka you can buy in the supermarket is mass-produced in a distillery on the scale of a petrochemical works. This is about using local produce and traditional methods to create a smooth drink.”38

Jamie spent considerable time sourcing the best possible distilling equipment, insisting on copper for the bespoke distillation column as well as the pot still that is used for the initial distillation. Every detail was researched and adjusted for maximum quality such as heating the still with a steam jacket rather than internal coils – the fermented mash still contains particulate matter that could burn on to the coils causing off flavours. A variety of yeasts were investigated and Jamie settled on ‘a variety that gives vodka flavours,’ keeping the identity secret.39

The English theme is maintained on the company’s website with its views of the rolling Herefordshire countryside and rousing intro music of Jupiter by Holst. Sponsorship of the James Bond, Quantum of Solace premiere in Herefordshire further emphasises this.

Chase was also able to publicise their English heritage during the visit of Oz Clarke and James May to the distillery as part of the BBC2 series, Oz and James Drink to Britain. This programme was aired on 10th February 2009

Chase has also aggressively pursued a strategy of entering – and winning – prestigious competitions around the world culminating in being voted ‘World’s Best vodka’ at the 2010 San Francisco World Spirits Competition beating P Diddy’s Cîroc into second place.

35 http://www.thetimes.co.uk/tto/life/food/article2673970.ece Times online 5th Aug 2010
36 Email correspondence 20/09/10
37 Times magazine 30/05/09
38 Times magazine 30/05/09
39 Conversation with Jamie Baxter during distillery visit 13th July 2010
Sales have maintained a steady increase since launch in 2008:-

Year end 2008 - £250,000  
Year end 2009 - £480,000  
Year end 2010 - £800,000  

With the recent entry into the US market, sales are predicted to continue healthy growth with Caroline Clarke estimating sales at:-

2011 - £1.5m  
2012 - £3m  
2013 - £5m  

The release of a Gin distilled from apples in January 2010, and range extensions such as the excellent Marmalade Vodka (Apr 2010) will continue to drive sales. The same focus on quality and Englishness is consistently in evidence with these products.

CONCLUSION

China is clearly going to be an important driver of growth in the premium category. It has a rapidly growing middle class that is becoming affluent and aspirational. With economic growth continuing at 7% annually, this trend is likely to continue. Whilst Baijiu remains extremely popular in the country, accounting for 99% of all spirits consumed, the increasingly affluent consumer is expected to offer significant opportunities for Western brands or premium Chinese versions of these brands such as Diageo’s Shanghai White, a premium vodka made in China that promotes its Chinese heritage. The younger generation are also more exposed to western drinking habits by internet and expat communities.

The problem with China is that Baijiu is already established with premium offerings and while there will undoubtedly be opportunities for western brands the growth in this category is not likely to be as large as expected.

However, India is generating significant excitement within the industry. They also have an enormous population that is growing rapidly and becoming increasingly wealthy. The difference is that the country already has a culture of drinking western style drinks particularly brown spirits and gin. According to Euromonitor data, China is expecting Vodka to show 11% CAGR over 2009-2014 but India is set for an incredible 21% CAGR over the same period.

The market is currently tightly regulated with punitive tax regimes on imported spirits which allows United Spirits to dominate domestically. The spirits market in India is 236m cases and United Spirits has a 59% share of this in the segments it operates in. They are also aggressively moving up the value chain for spirits. They estimate more than 100 million consumers will enter the legal drinking age in the next 5 years with 50% of the population below age 30, creating tremendous opportunity.

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40 Spirits Business Apr 2010  
41 Daily Telegraph 24th August 2010  
42 Diageo Premiumisation Seminar 16 Apr 2010  
43 Drinks Business Nov 2009
for growth.\textsuperscript{44} There will be premiumisation from local spirits to international brands and then once established, there’s further premiumisation within those international spirits.\textsuperscript{45}

Vodka has been the main driver behind the premiumisation of white spirits with its innovative production methods, ground-breaking marketing techniques and more recently with flavour extensions. However the global financial crisis of 2008-10 has caused a polarisation of the category with cash strapped consumers trading down to cheaper value brands and the premium offerings retaining their momentum within the upper socio-economic groups.

The vodka market has therefore become more competitive and the growth of ultra-premium lines has slowed from about 20\% to 5\% a year.\textsuperscript{46} Bling will become less important and consumers will demand a high quality drink that is well packaged. The western market may be reaching saturation point and there will certainly be some casualties but the large companies will continue to innovate and aggressively promote existing and new premium brands. Andy Fennel of Diageo does not see the market as cyclical, rather that trading up is a structural aspect of consumer categories.\textsuperscript{47} The market is unlikely to decline but growth will be much lower than it has been.

While the vodka market may be reaching maturity in western markets, it is likely that gin, tequila and white rum will continue their premiumisation journey as they are still significantly behind vodka in terms of sales and establishment of the trend. Consumers introduced to the premium category by vodka brands are showing signs of experimenting with more flavourful spirits and will naturally gravitate to the premium offerings. Combined with the growth opportunities in the Far East, it is clear that growth in the premium sector will continue for some considerable time yet.

\textsuperscript{44} Spirits Business May 2010
\textsuperscript{45} Andy Fennell, Just drinks interview 27/04/10
\textsuperscript{46} Drinks Business – Finance on Friday 28/06/09
\textsuperscript{47} Just drinks interview 27/04/10
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