Restructuring announcements by large companies within the Scotch Whisky industry over the summer of 2009 have brought the industry under the public and political spotlight. In response, the Economy, Energy and Tourism Committee is considering holding an inquiry into the industry. This briefing is intended to provide the Committee with an insight into the current state of the Scotch Whisky industry.

First, it takes a look at the main companies and summarises the economic impact of the industry in Scotland in terms of employment, income and exports.

The legal framework within which the Scotch Whisky industry operates is also outlined, with a particular look at the upcoming Scotch Whisky Regulations 2009 and the existing law with regard to the bottling of Scotch Whisky.

The briefing goes on to take a broad overview of the current domestic and international spirits market, with a specific look at the position of Scotch Whisky amidst other spirit drinks such as vodka.

Trends within the worldwide whisky market, such as the growth of regional brands and premiumisation, are then examined in more detail, before the key challenges currently facing the industry are outlined.

Lastly, Annexes 1 and 2 provide a summary of the restructuring plans announced by Diageo and Whyte & Mackay in recent months.
EXECUTIVE SUMMARY

The Scotch Whisky industry

Scherie Nicol

Scotch Whisky has been defined in UK law since 1909 and recognised in EU legislation since 1989. For a whisky to be labelled Scotch Whisky it has to be produced and matured in Scotland for a minimum of three years.

In Scotland, around 41,000 jobs directly or indirectly rely on the Scotch Whisky industry. Included in this is employment within bottling, packaging and distribution which together account for a greater proportion of employment in the spirits industry than employment in distilling itself. Whisky is one of Scotland’s top exporting sectors and is sold in over 200 countries worldwide.

Within the domestic market recent years have seen vodka overtake Scotch blended Whisky in sales volumes. However, sales of Scotch Whisky are growing in many overseas markets, such as Eastern Europe. In addition, there has been growth of regional/local whisky brands in markets such as India and this provides opportunities for Scotch malt Whisky to capitalise on premiumisation trends as disposable incomes increase in these countries.

Key challenges facing the Scotch Whisky industry include trade barriers, social responsibility issues and the image of the drink in the domestic market. Recent restructuring announcements by Diageo and Whyte & Mackay have also brought to the fore questions regarding the future of the industry in Scotland, and in particular the issue of foreign ownership and the potential for increasing quantities of Scotch Whisky to be bottled overseas.

### The Scotch Whisky industry – key numbers

<table>
<thead>
<tr>
<th>Number of distilleries (2009)</th>
<th>109</th>
<th>Sources:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct employment (2008)</td>
<td>9,300</td>
<td>SWA 2009a</td>
</tr>
<tr>
<td>Direct, indirect &amp; induced employment (2001)</td>
<td>41,000</td>
<td>SWA 2009a</td>
</tr>
<tr>
<td>GVA (2007)</td>
<td>£1.7bn</td>
<td>DTZ Pieda Consulting 2003</td>
</tr>
<tr>
<td>Exports (2008)</td>
<td>£3.1bn</td>
<td>Scottish Government 2009a</td>
</tr>
<tr>
<td>Average retail price of 70cl bottle (2008)</td>
<td>£13.37</td>
<td>SWA 2009c</td>
</tr>
<tr>
<td>Duty per 70cl bottle (2009)</td>
<td>£6.34</td>
<td>HMRC 2008</td>
</tr>
<tr>
<td>Duty per unit in the UK (2009)</td>
<td>£0.23</td>
<td>HMRC 2009</td>
</tr>
</tbody>
</table>
OVERVIEW OF THE SCOTCH WHISKY INDUSTRY

Whisky has been produced in Scotland for over 500 years. There are now over 102 working malt distilleries in Scotland and 7 grain distilleries. While malt distilleries produce whisky in batches using only malted barley, grain distilleries use a Coffey or Patent Still to allow continuous production of grain whisky using unmalted and malted barley together with other cereals. Some grain distilleries separately produce neutral alcohol for white spirits. The process of producing Scotch Whisky includes:

- barley/maltings
- distillery operations
- maturation & warehousing
- blending

- bottling & packaging
- transport & distribution
- advertising & marketing

The distilling industry has strong links with rural areas, such as Islay and Speyside where primary agriculture activities or distilling take place. Operations further down the supply chain such as bottling & packaging tend to be located in urban areas, such as Glasgow, Broxburn and Livingston. Approximately 15% of Scotch Whisky is bottled overseas. In addition, within some larger drinks companies operations such as advertising and marketing are also undertaken overseas. The Scotch Whisky industry is an international industry and Scotch Whisky has a huge international appeal, being sold in over 200 countries throughout the world (Scotch Whisky Association 2009a).

In 2005 the whisky industry agreed to formally define Scotch Whisky into five categories:

- **Single Malt Scotch Whisky** - distilled at a single distillery (i) from water and malted barley without the addition of any other cereals, and (ii) by batch distillation in pot stills. It is proposed that this type of whisky should only be bottled in Scotland.

- **Single Grain Scotch Whisky** - distilled at a single distillery (i) from water and malted barley with or without whole grains of other malted or unmalted cereals, and (ii) which does not comply with the definition of Single Malt Scotch Whisky.

- **Blended Scotch Whisky**: a blend of one or more Single Malt Scotch whiskies with one or more Single Grain Scotch whiskies.

- **Blended Malt Scotch Whisky**: a blend of Single Malt Scotch whiskies, which have been distilled at more than one distillery.

- **Blended Grain Scotch Whisky**: a blend of Single Grain Scotch whiskies, which have been distilled at more than one distillery (Scotch Whisky Association 2005).

The maturation process for whisky is a minimum of three years, but Scotch malt Whisky is often matured for ten years, and frequently longer. This means that distillers must currently set levels of production to meet what they estimate to be the level of demand over the next decade.

The fact that new capital investment in the whisky sector is at its highest level since the early 1970s is testament to the confidence investors have had in recent years with regard to the future market for whisky. The Scotch Whisky Association (SWA) estimate that there has been over £500m new investment in production capacity – including distilling, bottling and warehousing – over the last two years. It includes that of new distilleries (e.g., Roseisle and Ailsa Bay), the expansion of existing distilleries (e.g., Glenmorangie, The Glenlivet and Cameronbridge) and former distilleries being brought back into production (e.g., Glenglassaugh and Braeval). In addition, there has been investment in the expansion of warehousing, such as John Dewar’s new site in the Douglas Valley and at The Macallan in Speyside (SWA 2009a).
MAIN COMPANIES

Although the industry has its roots in local independent distillers, in today’s industry the distilleries, warehouses, bottling plants and distribution operations are owned by a range of companies, from large international plcs to family businesses owning a single malt distillery.

As a result of this shift, production is now dominated by a number of large multi-national drinks conglomerates – including Diageo, Pernod Ricard, William Grant & Son and the Edrington Group. These four companies own 62% of the distillation capacity for malt whisky and 85% of the distillation capacity for grain whisky. The remaining capacity is owned by a mixture of foreign and indigenous Scottish companies. Tables 1 and 2 summarise the ownership of distillation capacity within the industry in 2008:

<table>
<thead>
<tr>
<th>Owner</th>
<th>% of distillation capacity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Diageo</td>
<td>27%</td>
</tr>
<tr>
<td>Pernod Ricard</td>
<td>18%</td>
</tr>
<tr>
<td>Wm Grant &amp; Son</td>
<td>9%</td>
</tr>
<tr>
<td>Edrington</td>
<td>8%</td>
</tr>
<tr>
<td>Bacardi</td>
<td>6%</td>
</tr>
<tr>
<td>Others</td>
<td>32%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Owner</th>
<th>% of distillation capacity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Diageo</td>
<td>44%</td>
</tr>
<tr>
<td>Wm Grant &amp; Son</td>
<td>19%</td>
</tr>
<tr>
<td>Pernod Ricard</td>
<td>12%</td>
</tr>
<tr>
<td>Whyte &amp; MacKay</td>
<td>12%</td>
</tr>
<tr>
<td>Edrington</td>
<td>10%</td>
</tr>
<tr>
<td>Loch Lomond</td>
<td>4%</td>
</tr>
</tbody>
</table>

Source: Gray 2009

Diageo

Headquartered in London, Diageo is the world’s leading premium drinks company and is the largest single producer of Scotch Whisky. Key whisky brands in Diageo’s portfolio include Johnnie Walker (No. 1 whisky in the world), Bells (No. 1 Scotch Whisky in the UK) and J&B (No. 1 Scotch Whisky in Europe). They also boast an array of what they term ‘Classic malts’, ‘Distillery malts’ and Hidden malts’ which include brands such as Lagavulin and Talisker.

Its operations in Scotland extend to four maltings, 28 malt distilleries, two grain distilleries and eight major warehousing and blending sites (Diageo 2009a). In addition, currently Diageo undertakes 95% of its Scotch Whisky bottling in Scotland (SWA 2009a) and produces Smirnoff Red, Tanquery Sterling, Captain Morgan, Archers Aqua, Smirnoff Ice, Gilby’s Gin, Gordon’s Gin and Tanquery Gin in Scotland. Packaging is focused at three plants: Leven in Fife - bottling white spirits, Ready To Drink products and Scotch malt Whiskies; Kilmarnock in Ayrshire - bottling the complete range of premium Scotch Whiskies; and Shieldhall near Glasgow - bottling Diageo’s high volume Scotch Whisky brands.

Currently, Diageo employs over 4,500 people in Scotland. However, in an effort to save £100m annually, Diageo is implementing a major restructuring programme. Restructuring plans within Scotland, announced on 1 July 2009, will consolidate packaging operations from three sites to two and result in an overall reduction of up to 500 employees in Scotland, bringing employment down to around 4,000 people (Diageo 2009b).

In the year to June 2009 Diageo reported a 2% increase in net sales and a pre-tax profit of £2.015bn (BBC 2009a). Managing Director Diageo GB Simon Litherland explained that strong brands such as Smirnoff had helped it outperform the market (off licence news 2009a).
Pernod Ricard

Pernod Ricard, headquartered in Paris, is the second largest wine and spirits company in the world and has grown through a series of acquisitions over the years. The Group’s activities are focused on 15 key brands, representing more than half of the Group’s profits. Their strategy focuses on premiumisation rather than driving volume. These include The Glenlivet, Ballantine’s and Chivas Regal (Pernod Ricard 2009a).

Pernod subsidiary ‘Chivas Brothers’ employs 1,600 staff across 32 sites in the UK, including 29 locations in Scotland. It operates 12 malt whisky distilleries and one grain facility. Paisley-based Chivas also has more than 300 bonded warehouses containing in excess of 6 million casks of Scotch Whisky.

The Paris-based group has shown confidence in their Scotch Whisky portfolio and recently substantially expanded their Glenlivet distillery in Speyside.

In the year to June 2009 Pernod Ricard reported that pre-tax profit from recurring operations was up 21% to £1.6bn (reported as 1.8bn Euros) and the Group share of net profit was up 13% to £829m (reported as 945 Euros) (Pernod Ricard 2009b). These strong results were largely attributed to strong sales from their recent acquisition – Absolut Vodka. Pernod Ricard has made it clear that Absolut is its number one priority in spirits (off licence news 2009a).

William Grant and Sons

William Grant & Sons, headquartered in Dufftown, is a family-owned business that has been producing Glenfiddich whisky since 1887. Other key brands in their portfolio include Grant’s, Balvenie and Monkey Shoulder. In 1999 they joined forces with The Edrington Group and bought Highland Distillers (William Grant & Sons has a 30% stake).

It is now the largest whisky distiller still under Scottish ownership. Since 2002 William Grant & Sons have also been producing their own new brands of spirits for the market including gin, rum and vodka (William Grant & Sons 2009a). Their whiskies and spirits are bottled and stored in Bellshill, North Lanarkshire. The company’s distribution network comprises wholly-owned, joint venture and third party distribution companies. William Grant & Sons also distributes brands for other drinks companies.

In 2007 the company earned pre-tax profits for the Group of £83.6m for 2007, up 7% on the previous year (William Grant & Sons 2009b).
The Edrington Group

The Edrington Group is also still under Scottish ownership and is headquartered in Glasgow. Unusually for the drinks industry, it is owned by a charitable family trust – the Robertson Trust. The Trust was established to ensure that the family businesses remained active and independent, and that it continued and extended the past support they had given to charities.

In 1999 Edrington acquired Highland Distillers with William Grant & Sons (The Edrington Group 2009a) to become a brand-led drinks company like Diageo, Pernod Ricard and William Grant & Sons. Edrington now produces over 60 different whisky products, including key brands such as The Famous Grouse, Cutty Sark, The Macallan and Highland Park, which are blended on the same site as their bottling operation in Glasgow. In 2008 Edrington also acquired a majority stake in Brugal Company in the Dominican Republic, marking its entry into the market for rum.

In the year to March 2009 Edrington’s profit before tax was £94.8m, up 30.5% on 2008 (9.7% excluding the Brugal brand) (The Edrington Group 2009b). Over the same period the Robertson Trust committed £9.9m to almost 500 charities (The Robertson Trust 2009).

THE SCOTCH WHISKY ASSOCIATION

There are two trade associations which represent the Industry. These are the Scotch Whisky Association (SWA) and the Malt Distillers Association of Scotland (MDAS). While MDAS is focused on the production side of malt distilling, the SWA has a broader role in the industry.

Its 55 members account for more than 95% of production and sales of Scotch Whisky. Paul Walsh, CEO of Diageo, was appointed Chairman of the SWA in January 2008, with Ian Curle, CEO of the Edrington Group, appointed Vice-Chair.

Much of SWA’s work involves the protection of Scotch Whisky worldwide and the SWA alone has five intellectual property lawyers working to protect the category. At any one time they are handling up to 70 legal actions and conducting hundreds of investigations into fake products. Other principal functions of the SWA are:

- To promote responsible attitudes to alcohol consumption
- To secure fair and equal access to international markets
- To tackle tax discrimination and secure appropriate regulation of the industry
- To promote Scotch Whisky as a quality product made from natural raw materials
- To represent the industry’s interests at governmental level both at home and abroad

Source: SWA 2009b
ECONOMIC IMPACT OF THE SCOTCH WHISKY INDUSTRY

EMPLOYMENT AND INCOME

Around 9,800 people are directly employed within SWA member companies in Scotland (which represents around 90-95% of the industry). Figure 1 shows how direct employment has changed over the last decade and indicates that up until 2006 the long-run trend was a slow reduction in the number of employees within the industry. There was a pick-up in employment in 2006 and 2007, but it fell again in 2008 (SWA 2009a). Employment within the related bottling, packaging and distribution sectors is much higher than it is within the whisky distilling sector itself.

Taking into account indirect and induced employment it is estimated that in total around 41,000 jobs rely on the Scotch Whisky industry and generate over £800m in income within the economy (DTZ Pieda Consulting 2003).

The latest figures show that the spirit drinks industry accounted for £1.7bn Gross Value Added (GVA) in 2007 – representing £195,900 GVA per employee, compared to £45,700 GVA per employee across all industries (Scottish Government 2009).

EXPORTS

Food, Drink & Tobacco (predominantly whisky) has historically been one of Scotland’s strongest exporting sectors by value. It was the top exporting sector until the early 1980s when the value of electrical engineering exports soared and has remained the second most valuable exporting sector to date. Whisky exports from Scotland in 2008 were valued at £3.1bn. As it is exported to over 200 countries worldwide, the value of Scotch Whisky exports tends to follow global economic trends. Figure 2 below shows that whisky exports dipped substantially in 1998 following the 1997 Asian Financial crisis:

![Figure 2: Export value of Scotch Whisky 1975 to 2008 (£m)](image)

Sources: SWA 2008, SWA 2009c
The SWA provides more detailed export statistics on the value of Scotch Whisky exports by destination. Data from the SWA indicates that the USA, France and Spain have consistently been the top three export markets for whisky over the previous decade. However, countries such as Singapore and South Africa have become increasingly valuable markets and in recent years emerging economies such as China and India have entered the top 20 destinations.

**Figure 3: Top ten destinations for estimated Scotch Whisky exports (£m) 2008**

<table>
<thead>
<tr>
<th>Destination</th>
<th>Value</th>
<th>Volume</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU (excl UK)</td>
<td>£1.28bn</td>
<td>441.9m bottles</td>
</tr>
<tr>
<td>Total exports</td>
<td>£3.06bn</td>
<td>1,080.3m bottles</td>
</tr>
</tbody>
</table>

Source: [SWA](#) 2009c
A CLOSER LOOK AT LINKAGES WITH OTHER INDUSTRIES

White Spirit Production
Some major drinks companies have consolidated their spirits production activity in Scotland. This has undoubtedly been influenced by the existence of the whisky industry which has created the necessary infrastructure, including production facilities and bottling capacity (DTZ Pieda Consulting 2003). It provides the opportunity for economies of scale, for example through the co-location of white spirits and whisky production or shared distribution channels. Around 2,300 jobs and £50m income is linked to the white spirits industry in Scotland. According to the Scottish Executive, in 2006 the UK was the second largest vodka producer in the EU after Poland (2006).

Agriculture
The Scotch Whisky industry has close linkages with the agriculture sector in Scotland with over £90m of cereals being purchased from Scottish suppliers (DTZ Pieda Consulting 2003).

In addition, distillers supply the agriculture industry with various forms of animal feed derived from the cereals and distillation residues and rely on the industry for the beneficial disposal of used cereals and distillery co-products onto agricultural land (Stevens View Partnership 2007).

Tourism
Research by Market Research Partners found that Scotch Whisky is by far the product most associated with Scotland (ScotlandWhisky 2005). Scotch Whisky, among other products such as golf and ancestry, gives Scotland an international profile and helps attract visitors to the country. The whisky industry is particularly important in drawing visitors to rural areas. According to ScotlandWhisky there are over 50 distilleries spread across five regional areas that can be visited in Scotland (2009).

ScotlandWhisky also released data showing that 1.2 million visitors toured a distillery in 2007 - a 2.6% increase over the last 3 years - and spent more than £22.4 million at whisky visitor attractions - a 17.8% increase over the last three years (ScotlandWhisky 2008).
LEGAL REQUIREMENTS WITHIN THE SCOTCH WHISKY INDUSTRY

DEFINITION OF SCOTCH WHISKY

Key UK legislation relating to Scotch Whisky includes the Scotch Whisky Act 1988 (c.22) and the Scotch Whisky Order made under it in June 1990. These make provisions with regard to the definition of Scotch Whisky and as to the production and sale of whisky. The Scotch Whisky Order 1990 states:

“For the purpose of the Act "Scotch Whisky" means whisky—

(a) which has been produced at a distillery in Scotland from water and malted barley (to which only whole grains of other cereals may be added) all of which have been—

(i) processed at that distillery into a mash;

(ii) converted to a fermentable substrate only by endogenous enzyme systems; and

(iii) fermented only by the addition of yeast;

(b) which has been distilled at an alcoholic strength by volume of less than 94.8 per cent so that the distillate has an aroma and taste derived from the raw materials used in, and the method of, its production;

(c) which has been matured in an excise warehouse in Scotland in oak casks of a capacity not exceeding 700 litres, the period of that maturation being not less than 3 years;

(d) which retains the colour, aroma and taste derived from the raw materials used in, and the method of, its production and maturation; and

(e) to which no substance other than water and spirit caramel has been added."

In addition, the 1988 Act, and the 1990 Order describe how Scotch Whisky must be a minimum alcoholic strength of 40% (in line with the current EC Regulation for whisky).

This protects consumers from being sold ‘Scotch Whisky’ products not complying with the legislation, and ensures Scotch Whisky’s reputation is not undermined.

SCOTCH WHISKY REGULATIONS 2009

In recent years, there have been calls from the Scotch Whisky industry for the Government to enhance the protection of Scotch Whisky. The UK Department for Environment, Food & Rural Affairs (Defra) has policy responsibility for the EC Spirit Drinks Regulation 110/2008 (see section on EU Legislation). At the time when Defra consulted on their proposals for the Spirit Drinks Regulations 2008, through which the EC Spirit Drinks Regulation is implemented, Defra also proposed new regulations on Scotch Whisky (a protected Geographical Indication under the EC Regulation) which would give additional protection to the industry, named the Scotch Whisky Regulations 2009. Defra stated that:

“The proposed Regulations will:

- Define five categories of "Scotch Whisky" (Single Malt Scotch Whisky, Single Grain Scotch Whisky, Blended Scotch Whisky, Blended Malt Scotch Whisky and Blended Grain Scotch Whisky) and will require these category names to be used.
- Allow the five "Scotch Whisky" categories to be supplemented initially by one of five regional names (Highland, Lowland, Speyside, Campbeltown, Islay). Further protected regions may be added to the Regulations at a later date. Products will not be allowed to use protected regional names if they have not been wholly made in the region.
• Prohibit whisky from being labelled with the name of a distillery or a similar name if it is not a product of that distillery.
• Prohibit labelling, packaging, presentation or advertising suggesting that a single malt was made at a distillery other than the actual distillery where it was made (e.g. using made up company names).
• Require all Scotch Whisky to be wholly matured in Scotland.
• Prohibit the export from Scotland of Scotch Whisky in wooden casks.
• Prohibit the export of Single Malt Scotch Whisky unless it has been bottled and labeled”.

Source: Scotland Office 2007

The proposals for both the Spirit Drinks Regulations 2008 and the proposed Scotch Whisky Regulations were put out to consultation on 31st December 2007. These Scotch Whisky Regulations 2009 are due to come into force on 30th November 2009 – St Andrews Day (Defra 2009).

OTHER LAYERS OF LEGAL PROTECTION

The Scotch Whisky industry uses the existence of the UK legislation in legal action overseas where ‘Scotch Whisky’ is defined by reference to UK Law. Scotch Whisky is also further protected in overseas markets under EU legislation and WTO agreements.

EC Legislation

Scotch Whisky has been recognised in EC legislation since 1989. It is currently protected at EU level by Regulation (EC) No 110/2008 of the European Parliament. It regulates the definition, description, presentation, labelling and protection of Geographical Indications of spirit drinks. With regard to whisky or whiskey it states:

“(a) Whisky or whiskey is a spirit drink produced exclusively by:
(i) distillation of a mash made from malted cereals with or without whole grains of other cereals, which has been:
— saccharified by the diastase of the malt contained therein, with or without other natural enzymes,
— fermented by the action of yeast;
(ii) one or more distillations at less than 94.8 % vol., so that the distillate has an aroma and taste derived from the raw materials used,
(iii) maturation of the final distillate for at least three years in wooden casks not exceeding 700 litres capacity. The final distillate, to which only water and plain caramel (for colouring) may be added, retains its colour, aroma and taste derived from the production process referred to in points (i), (ii) and (iii).
(b) The minimum alcoholic strength by volume of whisky or whiskey shall be 40%.
(c) No addition of alcohol as defined in Annex I (5), diluted or not, shall take place.
(d) Whisky or whiskey shall not be sweetened or flavoured, nor contain any additives other than plain caramel used for colouring”.

Council Regulation (EC) No 510/2006 of 20 March 2006 on the protection of Geographical Indications and designations of origin for agricultural products and foodstuffs also lists Scotch Whisky as a protected Geographical Indication (GI), along with four other whiskies - Irish Whiskey, Whisky Español, Whisky de Bretagne and Whisky d’Alsace. As a protected GI, a named food or drink registered at a European level will be given legal protection against imitation throughout the EU. ‘Scotch’ is designated a GI only to be used for whisky produced in Scotland.
In order to obtain a protected GI, agricultural products or foodstuffs must comply with the product specification, which must include the following aspects:

- the name of the GI;
- the description of the product, with an indication of its main physical, chemical, microbiological and organoleptic properties;
- definition of the geographical area;
- information proving that the product originates from that area;
- information justifying the link between the product and the geographical area;
- description of the production method and, if appropriate, the authentic and unvarying local methods as well as information concerning packaging that takes place in the defined geographical area in order to safeguard quality, ensure the origin or ensure control;
- the name and address of authorities or bodies that verify compliance with the provisions contained in the product specification;
- any specific labelling rule for the product in question;
- any requirements laid down by Community or national provisions.

Source: Europa 2009

The use of designated GI terms is regulated by Defra.

**World Trade Organisation**

Scotch Whisky is also protected by the World Trade Organisation (WTO) as a recognised ‘geographical indication’ through the TRIPS (trade-related aspects of intellectual property rights) agreement. The TRIPS Agreement is an attempt to narrow the gaps in the way these rights are protected around the world, and to bring them under common international rules.

**WHISKY LEGISLATION – WHO’S DOMAIN IS IT ANYWAY?**

Legislation regarding the legal definition of Scotch Whisky could be passed by the Scottish Parliament; however, in line with the Scotland Act 1998 any legislation agreed by the Scottish Parliament would need to comply with EU law where Scotch Whisky is defined. It would also have to cover matters that do not fall within the reserved areas set out in Schedule 5 to the Scotland Act. While issues such as labelling could be within the legislative competence of the Scottish Parliament, others such as the legal definition of whisky are unlikely to be given that such provisions will be in the areas of intellectual property (copyright), export control and consumer protection, all of which are reserved matters.

Additionally, the Defra Food Policy Unit has policy responsibility for implementing the EC Spirit Drinks Regulation 110/2008 in the UK, and does so through the Spirit Drinks Regulations 2008. This may be further indication that the legal definition of Scotch Whisky is reserved to Westminster in legislative terms.

It is as a result of this legislative context, as well as the need for the regulations to apply across the whole of the UK, that Defra has been drafting the consultation document and draft regulations for the Spirit Drinks Regulations 2008 and the Scotch Whisky Regulations 2009.
BOTTLING OF SCOTCH WHISKY

There is no law requiring Scotch Whisky to be bottled in Scotland – although as previously mentioned there are proposals within the Scotch Whisky Regulations 2009 to introduce this law with regard to Scotch malt Whisky.

In the case of Scotch Whisky, to stipulate the geographical location where a product is packaged through an EU Geographic Indication, it would need to be proven that the bottling of Scotch Whisky in Scotland is necessary to safeguard quality, ensure the origin or ensure control.

Scotch blended Whisky

Scotch blended Whiskies have been exported in bulk for around a century - to be bottled in countries such as the USA, Brazil and France. The SWA believe that there are reasons for this practice to continue:

1. Many countries demand bulk supplies of whisky to be blended with other whiskies and locally branded. If bulk supplies of Scotch Whisky were not used in these local blends then it is likely that bulk supplies of whisky would be sourced from other whisky exporting countries.

2. In some countries the local fiscal and regulatory framework makes market access easier for bulk rather than bottled products. For example, several countries in South America apply lower taxes to bulk shipments. If Scotch Whisky was not exported in bulk to these countries it would be more difficult to compete with products exported from other whisky producing countries on a price basis.

3. If the exporting of Scotch blended Whisky in bulk was made unlawful, given that the existing trade in bulk shipments of Scotch blended Whisky support a number of bottling jobs in overseas countries, any new requirement to bottle blended whisky in Scotland would likely result in challenge by third country Governments. This occurred when Mexico attempted to stipulate that all tequila must be bottled in Mexico. The USA was prepared to approach the WTO regarding these proposals and in the end they were withdrawn (SWA 2009a).

However, there are also those who believe that all Scotch blended Whisky should bottled in Scotland to preserve the reputation of the industry (through retaining the link between the whisky and its history) and to safeguard direct employment at the bottling plants alongside indirect employment within companies located in Scotland to undertake supply-chain activities such as glass manufacture, labelling, inspection, etc. The Scottish Council of Development and Industry (SCDI) published a discussion paper ‘Should Scotland Export Bulk Whisky?’ in 1979. The paper concluded that Scotland would economically benefit in the long-term if the bulk export of all whisky was banned. SCDI has more recently stated that, to protect Scotch Whisky’s reputation, should the quantities of Scotch Whisky shipped in bulk abroad fall in the future, it may become feasible to revisit the bulk export of Scotch blended Whisky (SCDI 2008).

Scotch malt Whisky

Unlike Scotch blended Whisky, less than 1% of exported Scotch malt Whisky is exported in bulk. The whisky industry in Scotland widely supports the requirement within the Scotch Whisky Regulations 2009 for all Scotch malt Whisky to be bottled in Scotland. It is believed that these regulations will be allowed under EU legislation and will not be opposed by countries outwith the EU for two reasons:

1. Given that Scotch malt Whisky relies on confidence in its purity and quality to generate sales the industry argues that bottling it in Scotland would ensure control of its quality. The SWA provided evidence to Defra that “exports of Scotch Whisky in bulk has led to adulteration and contamination when it is bottled abroad. This risks damaging the
reputation of Scotch Whisky and leaves consumers vulnerable to counterfeit products which could also have public health implications” (Defra 2008). They see this regulation as important to help protect the quality of Scotch malt Whisky and prevent any future problems arising around the misuse of bulk Scotch malt Whisky exports.

2. Only a very small volume of Scotch malt Whisky is currently exported for overseas bottling, and the new rule will have a negligible impact on current employment within overseas countries (SWA 2009a).

PROTECTION OF BOTTLING OF OTHER PRODUCTS

There are some examples of alcohol products within the EU where legislation exists to ensure they are bottled within a defined geographical area.

Wine

Within the wine industry today there is, in general, no legal requirement to bottle at source, however there are some exceptions. One wine for which such a legal requirement still exists is Rioja.

Rioja

The Spanish Government regulates the quality, ingredients and production process of Spanish food and drink. A regulator exists for each region and, thus, the Spanish Government viewed it necessary to enable the regulator to supervise production and ensure the quality for any wine from that region to be bottled within the same region. In 1989 the EC Court stated that these Spanish provisions which limited the bulk export of wine had the equivalent effect of a quantitative restriction on exports – prohibited within Section 34 (now 29) within the EC Treaty.

In response the Spanish Government amended their provisions to rule that bottling had to take place only in authorised bottling plants. In the case of Rioja, wine bearing the words ‘*Rioja denominacion de origen calificada*’ (Rioja wine of designated origin) could only be bottled within authorised cellars within La Rioja region. Belgium, supported by the UK, subsequently began legal proceedings against Spain for breaching Section 34 of the EC Treaty.

However, the EC Court agreed with Spain that the bottling was not merely filling containers but involved several processes which had to be undertaken within the prescribed rules of trade to uphold the quality and maintain the characteristics of the wine. This is more likely to be assured if it is done by established operations within the region that have specialist knowledge and experience of the strict requirements. The Spanish regulations were therefore upheld and current Spanish law states that Rioja wine must be bottled at cellars within La Rioja region to qualify for ‘*Rioja denominacion de origen calificada*’ status (O’Connor 2004).

Note there is no prohibition on the export of bulk wine from La Rioja region if it is not branded as ‘Rioja’.

French wine

Other wines use labeling practices to help protect the quality of their products. For example, the labels on a bottle of French wine often carry information about bottling (whether it was bottled at the vineyard, in the general estate or in a different place from where the grapes were grown) that can help the consumer evaluate its quality. However, it is worth bearing in mind that any labeling legislation introduced in the UK would need to comply with the existing UK Food Labeling Regulations 1996. Spirit drinks labeling is also regulated by the EU.
**Cognac**

Cognac faces challenges in appealing to younger drinkers in its home market, who tend to prefer Scotch Whisky. However, the same cannot be said for export markets and Cognac is now exported to over 150 countries, with individual markets such as the US, the UK and Spain particularly valuable to the industry. Heavy dependence on these markets, particularly on the US market, saw the volume of Cognac sales fall during the recent economic downturn.

The world’s leading four brands of Cognac are Hennessy, Remy Martin, Martell and Courvoisier ([Drinks International](https://www.drinksinformation.com) 2009). Alongside large-scale suppliers, many independent grower-bottlers also exist within the industry.

Like Scotch Whisky, Cognac is protected by a legal framework that preserves the authenticity and uniqueness of the drink. Those who fail to respect its regulations are not allowed to use the name of the ‘controlled appellation of origin Cognac’. The stages involved in Cognac production subject to regulations include the area of production, grape varieties used, vinification, distillation, alcohol content, additives, storage & ageing and labelling ([Cognac.fr](https://www.cognac.fr) 2009).

The French Government has passed an enabling law permitting compulsory bottling at source for Cognac and Armagnac products. However, it is not believed that any regulations have yet been introduced (SWA 2009a).

**Outwith the EU**

Outwith the EU there are examples of other products where protection applies to the packaging of products. For example, under Mexican law all 100% agave or aged Tequila must be bottled in Mexico. In addition to this, Mexico attempted to introduce a bi-lateral trade agreement with the US requiring all Mexican tequila to be bottled in Mexico. However, this was opposed by the US and, ultimately, the [2006 Tequila Trade Agreement](https://www.fas.usda.gov/) between the two countries allowed the US to continue importing tequila in bulk for bottling. Despite this, the agreement created a registry which identified approved bottlers of tequila and an agency to monitor this.
AN OVERVIEW OF THE SPIRITS MARKET

UK
The UK is one of Europe’s most valuable spirit markets. Neilsen’s off-trade Scantrack Service, which monitors weekly sales from a network of nationwide checkout scanners, estimated the value of the off-trade spirits market in the UK as £3bn in the year to August 2009 – up 7% on the previous year. The volume of spirits sold rose 2% over the year. Coverage includes grocery multiples, co-ops, multiple off-licences, independents, symbol groups and multiple forecourts.

The results also show that for the second year running vodka has surpassed blended Scotch Whisky as the favourite category within spirits for take home shoppers. Vodka accounts for £863m - over a quarter of the value of overall spirit sales – whereas blended Scotch Whisky accounts for £782m. However, this still represents almost £1 in every £6 spent on spirits. It is thought by industry analysts that it is Scotch Whisky’s difficulty in appealing to a younger drinker, relative to vodka, that is likely to have caused the sales swing to the latter.

In the UK, the five most popular Scotch blended Whiskies are Bell’s (Diageo), The Famous Grouse (Edrington), High Commissioner (Glen Catrine Bonded Warehouse), William Grant’s (William Grant & Sons) and Teacher’s (Beam Global). Although the value of Scotch blended Whisky sales rose 4% between 2008 and 2009, the volume of sales fell 1% (off licence news 2009b).

Similarly, the value of Scotch malt Whisky sales rose 3%, but the volume fell 2%. The five most popular Scotch malt Whiskies are Glenmorangie Original (Louis Vuitton Moet Hennessy), Glenfiddich (William Grant & Sons), The Glenlivet (Pernod Ricard), Aberlour (Pernod Ricard) and Laphroaig (Beam Global) (off licence news 2009b).

Interestingly, it was imported whisky (headed by Bacardi-owned Jack Daniel’s) that had the strongest growth in sales value in the overall spirits sector over the year to August 2009 (12%), followed by vodka (10%). Within this category, value brands have also seen high growth. off licence news wrote that “shoppers seem to be trading down to less expensive versions of their preferred brands or to cheaper brands altogether” (2009b).

INTERNATIONAL
As a result of the prevailing economic downturn there is some evidence within the worldwide spirits market of reduced demand and trading-down to cheaper products in countries particularly badly hit by the recession, such as the US, the UK, Ireland and Spain. For example, leading cognac brands, which rely heavily on sales in the US and the UK, have experienced a fall in demand, as have high-end vodka brands in the US as a result of trading-down. Another trend emerging as a result of the recession is a switch from on-trade sales (i.e. sales within bars, hotels & restaurants) to off-trade sales (i.e. retail sales) as consumers become more value conscious (Drinks International 2009).
Despite these trends, the worldwide spirits market is still judged by market analysts as performing well given the economic conditions. This is largely attributed to strong brands and growing sales in emerging markets. For example, strong growth in central and Eastern European markets has benefited the Scotch Whisky industry throughout this period.

According to data from Euromonitor International, whisky accounts for 12% of the worldwide spirits market by volume, as shown in Figure 5. It is the second most dominant spirit in the market, after white spirits, which account for 23% of market volumes. It should be noted that a lot of the white spirits markets are domestic, in contrast to whisky which is extensively internationally traded.

**Figure 5 – Proportion of worldwide spirits market by volume, 2008**

<table>
<thead>
<tr>
<th>Spirit Type</th>
<th>Market Share by Volume (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>White spirits</td>
<td>23%</td>
</tr>
<tr>
<td>Whisk(e)y</td>
<td>12%</td>
</tr>
<tr>
<td>Rum</td>
<td>7%</td>
</tr>
<tr>
<td>Brandy &amp; Cognac</td>
<td>6%</td>
</tr>
<tr>
<td>Liqueurs</td>
<td>5%</td>
</tr>
<tr>
<td>Tequila</td>
<td>1%</td>
</tr>
<tr>
<td>Other spirits</td>
<td>46%</td>
</tr>
</tbody>
</table>

Source: [Drinks International](http://www.drinksinternational.com) 2009

Within the premium spirit market, vodka is undoubtedly the star performer with data from Impact Databank showing four of the top five growth brands in 2008 being vodka drinks – all showing sales growth of over 20% (Impact 2009). It is a fast-changing market and, although Smirnoff is the clear leading brand, new players are continually emerging and there is considerable churn in the most popular brands. Intangible Business, which produces the Fortune 100 publication rating the most powerful brands in the wine and spirits market, stated:

“The vodka market has surpassed all expectations. Led by Smirnoff, Absolut and others including Grey Goose, Stolichnaya, Skyy and Finlandia, the whole category continued to grow when it had looked like growth was stalling. This underlines vodka’s power in the market, fueled by powerful branding, its versatility as a cocktail and mixer ingredient, its alignment with sophisticated marketing programmes and its capture of a still buoyant US market which may come under threat as the recession takes hold” (2009).

Nevertheless, vodka is not necessarily Scotch Whisky’s biggest competitor – this depends on the market – and Scotch Whisky is still showing growth, with Impact Databank data showing sales volume of key brands such as Johnnie Walker, Ballantine’s, Grant’s and Chivas Regal growing 3-6% over the year (Impact 2009).

While whisky is behind white spirits, and vodka in particular, in terms of worldwide sales volume, the higher price that it commands at the premium end of the market means that it is leading in terms of sales value. Johnnie Walker’s positioning at the high end of the market also means that in terms of sales value it is the top spirit brand in the world. Within their 2009 report, Intangible Business rate whisky as the top sector in terms of its ability to generate value for its owner, followed by vodka ([Intangible Business](http://www.intangiblebusiness.com) 2009).
WORLDWIDE TRENDS IN THE WHISKY INDUSTRY

CONSOLIDATION AND DIVERSIFICATION
The last decade has brought much consolidation within the drinks industry. In addition, recent years have seen Scotch Whisky companies expand beyond their traditional business. For example, William Grant & Sons recently launched Sailor Jerry rum and Hendrick’s gin. Edrington has expanded into the market for other spirits too, through the acquisition of the Caribbean rum Brugal. Likewise, Scotch Whisky brands have been acquired by larger foreign drinks companies looking to diversify their portfolios. Consolidation and diversification has allowed companies to expand their consumer base and also makes them less exposed to volatility in a single market. However, the consolidation has also resulted in the rationalisation of head office functions in Scotland and the relocation of some positions to global headquarters.

GROWTH OF REGIONAL AND DOMESTIC/LOCAL BRANDS
The global spirits market is founded upon domestic/local brands which account for more than half the volumes of worldwide spirits sales (Drinks International 2009). Local whiskies are showing strong growth in sales volume and may soon begin to dominate sales volume in the market for whisky. For example, Bagpiper, an Indian whisky, sold 15.4 million cases worldwide in 2008, compared to Johnnie Walker’s 16.3 million and, if it continues growing at the same pace, it will overtake Johnnie Walker in sales volume next year (Impact 2009). The SWA does not see these brands as a threat as they believe these brands help nurture local roots, enabling the development of a sales infrastructure that can sustain international brands later (SWA 2009a). However, there is always the risk that the threat of new brands is under-estimated.

PREMIUMISATION IN BOTH EMERGING AND MATURE MARKETS
As disposable incomes rise in emerging markets, such as the BRIC countries (Brazil, Russia, India and China), there is the opportunity to steer these customers towards premium Scotch Whisky. This is already happening in China where Scotch Whisky consumption is growing at an annual rate of 19% (Lloyd-Jones 2003). Within mature markets such as the UK, premiumisation is also a key strategy within the Scotch malt Whisky industry to enable it to sell products with higher profit margins. Companies are making investment to tap into this market through introducing new premium products and repositioning existing brands. For example, Diageo has introduced a new branding – 'The Singleton' – for several of its smaller malt brands making them easier to identify as single malt whiskies with the aim of attracting new customers into this category.

GROWING IMPORTANCE OF THE ASIA-PACIFIC MARKET
Although markets such as the US, France and Spain are the most valuable for the Scotch Whisky industry, Asia-Pacific is still the key region in terms of volume of consumption. In 2008, the region accounted for 49% of total spirits consumption. The next biggest region was North America (20%), Western Europe (19%) and Latin America (6%) with Middle East & Africa, Eastern Europe and Australia all accounting for less than 5% each (Drinks International 2009).

With disposable incomes rising in the Asia-Pacific region it offers good growth prospects to the spirit market. However, the economic environment in this region also has the potential to negatively impact sales volumes of Scotch Whisky. For example, in 2004 an economic downturn in South Korea meant that overall export volumes of Scotch Whisky to Asia were down 14% (Beveragedaily.com 2004).
KEY ISSUES FOR THE INDUSTRY

PERFORMANCE OF SCOTCH WHISKY IN UK MARKET
Within the UK, Scotch Whisky is predominantly drunk by males and those aged over 30. Off license news believes that “blended whisky producers will need to pull out all the stops if the spirit is to become the best-selling spirit in the off-trade again. Some funky packaging makeovers and some unique, up-to-date marketing campaigns are what’s needed to turn blended whiskies fortunes around.” (Off license news 2009b).

The under-performance of Scotch ‘own label’ blended Whiskies within the UK volume/value market place contrasts with the strong performance of companies favouring an international premiumisation strategy – particularly for Scotch malt Whisky.

INCREASED COMPETITION FROM OTHER SPIRITS
The high levels of growth seen with white spirits and particularly vodka in certain countries, such as the UK and US, pose a challenge to the whisky industry. In addition, internationally produced whiskies such as those from Canada and Japan are gaining increased sales in some markets. Nevertheless, just as imported spirits are gaining market share in the UK, whisky is an attractive import relative to other spirits in markets such as South Africa and Eastern Europe.

LEGAL PROTECTION
The industry has lobbied hard for specific trademark protection across the globe, conscious that the premium nature of the product means it is particularly vulnerable to counterfeiters. The proposed Scotch Whisky Regulations 2009 which will define Scotch Whisky into five categories and the existence of this new legislation is aimed to help the SWA to take action against foreign counterfeiters.

TRADE BARRIERS
The SWA reports that, of the 200 countries in which Scotch Whisky is sold, it faces over 600 trade barriers in 143 of these. Discrimination most commonly takes the form of high duty on Scotch Whisky relative to other (in certain instances locally produced) products. Other forms of barriers include advertising restrictions, profit margin controls, health warnings, minimum values for duty/tax purposes, quotas and labelling restrictions. The SWA, the UK Government, the EC and the WTO work hard to eliminate discrimination through trade barriers. Successful examples include that of Taiwan, where tax discrimination was removed in 1999 resulting in the retail price of Scotch Whisky falling 25% (Gray 2008).

SOCIAL RESPONSIBILITY ISSUES
Increased awareness of the health and social costs related to alcohol misuse, together with changing patterns of drinking – such as binge drinking - have brought increased concern with regard to the current ‘drink culture’ in the UK. There is growing pressure to implement further measures to prevent alcohol misuse. For example, the British Medical Association is calling for a complete ban on alcohol advertising, blaming it for the growing alcohol consumption, particularly among young people (British Medical Association 2009).

The Scotch Whisky industry has introduced a Code of Practice, setting out minimum standards for marketing and promotion within the UK and best practice in international markets, to show its commitment to promoting responsible drinking.
Minimum Pricing

As part of their 2009-10 legislative programme the Scottish Government will introduce a Bill to Tackle Alcohol Misuse. The Government recognises alcohol misuse as a significant problem in Scotland and estimates that it costs Scotland £2.25 billion per year in extra services and lost productivity (Scottish Government 2009b). One of the key instruments within the Bill will be a minimum pricing policy for alcohol. A study undertaken by the University of Sheffield on behalf of the Scottish Government shows that:

"Using an example minimum price of 40p per unit combined with a ban on promotions, alcohol-related deaths would fall by about 70 in the first year of the policy and about 370 per year after 10 years of operation - a drop in such deaths of nearly 20 per cent. It also shows that a minimum pricing policy would lead to significant falls in alcohol-related illnesses and crimes, leading to yearly savings for taxpayers. It would also have economic benefits - including nearly 30,000 fewer absence days from work every year, using the 40p example with a promotions ban" (Scottish Government 2009c).

The report also states that the greatest impact of the policy will be on heavy drinkers, who tend to choose cheap, higher-strength products such as white cider and own label spirits.

Figure 6 provides information on how duty per unit of alcohol currently varies between different alcoholic drinks.

Source: House of Commons Library 2009

The minimum pricing legislation, like any other alcohol policy, must take into account obligations in relation to:

1. International and European law
2. Other policies dealing with alcohol as an economic commodity
3. International actions to reduce the harm done by alcohol

When considering whether or not health policies on alcohol comply with legal obligations, the EU states that "Health policymakers should ensure that health policies interfere with trade as little as possible, and should monitor the risks inherent in the process of trade liberalisation, especially at the global level" (Policy in Europe 2006). It also states that:

"Member States do have flexibility in setting the relative taxes on drinks but not to the extent that they can attach a greater tax to drinks only produced abroad.... A similar conclusion has been reached on the legality of minimum pricing agreements, which may be ruled illegal where they stop low-price competition from abroad" (Policy in Europe 2006)

The SWA, representing the whisky industry, supports most of the Government’s proposals but is opposed to the introduction of Minimum Pricing for reasons including the following:

- With 30% of Scotch Whisky sales in Scotland being through supermarket own label and ‘cheapest on display’ brands and 50% of sales in Scotland taking place when Scotch Whisky is on promotion, the industry believe that as a result of this policy the price of Scotch Whisky would rise and sales would decline - putting more pressure on jobs within the industry, particularly at firms heavily dependent on the domestic market such as Whyte & Mackay.
- They speculate that the policy would encourage other countries to consider introducing spuriously-based ‘public health’ measures which could purposefully or not discriminate
against imported Scotch Whisky. For example, through introducing a health tax that would apply to spirits over 30% alcohol by volume. The Scotch Whisky industry also believe that fighting these restrictive trade policies based on ‘public health’ concerns would be more difficult if the Minimum Pricing Policy is in operation in Scotland on the grounds of public health. Therefore, this policy would lead to difficulty fighting protectionist policies from other countries which would negatively impact exports of Scotch Whisky (SWA 2009a).

The Economy, Energy & Tourism Committee may wish to explore further how the Minimum Pricing proposals could impact the Scotch Whisky industry.

PERCEPTION OF INDUSTRY WITHIN SCOTLAND

Foreign ownership

The proportion of distilleries under foreign ownership has increased from 22% in 1980 to 40% now (Gray 2008). In addition, of those which remain under UK ownership, the proportion retained by small independent operators has fallen while the proportion owned by the larger firms has increased.

Increased foreign ownership can bring with it the transfer of central functions, such as management and marketing, to international corporate headquarters. In addition, the recent restructuring announcements at Diageo and Whyte & Mackay have increased the perception that pressures to make profit mean that these companies are not as committed to Scotland as indigenous Scottish companies and that strategic decisions taken outwith Scotland do not take as much consideration of the impact they may have on potentially fragile local economies.

However, the SWA believe that their companies are acutely aware of the role they play in Scottish communities, but that difficult decisions have to be made when operating from a high cost base in a challenging global market (SWA 2009d). In addition, it points to the high levels of investment that these larger companies have put into the Scotch Whisky industry in recent years as well as the benefits that their large marketing budgets can bring to the industry as a whole through creating a market for and raising awareness of Scotch Whisky across the world.

Movement of bottling operations overseas

It is currently estimated that 15% of Scotch Whisky is bottled overseas. Whyte & Mackay, for example, bottle Scotch Whisky for domestic Indian consumption at its plant in Western India. This figure is lower than what it was in 1998 (21%). However, recent redundancy announcements by Diageo and Whyte & Mackay have indicated the pressures that international drinks companies are under to cut costs in this period of economic uncertainty. The decision by Diageo to move the bottling of Johnnie Walker out of Kilmarnock, has also been viewed as an indication that there is less emphasis being placed on Scotch Whisky’s historical links with a certain area. Both of these factors have brought with them speculation that in coming years the proportion of Scotch Whisky bottled overseas, closer to key markets, may increase.

Given that the white spirits industry in Scotland relies on the economies of scale provided by the whisky bottling infrastructure, any movement of whisky bottling operations overseas would also raise questions about the viability of white spirits bottling operations in Scotland. This would in turn impact on the viability of other supply-chain operations located in Scotland, including the manufacture of glass, closures, tubes, labelling, packaging, inspection, warehousing and distribution – many of which are owned by foreign investors. Therefore the movement of whisky bottling overseas would be a major threat to the future of the white spirit industry and corresponding supply-chain businesses in Scotland.

The movement of bottling overseas and its potential impact on the Scottish economy may be an area which the Economy, Energy & Tourism Committee may wish to explore further.
ANNEXE 1 - SUMMARY OF DIAGEO’S RESTRUCTURING PROPOSALS

Diageo’s Scottish restructuring plans announced in July 2009 target annual cost savings of £42 million. The restructuring programme comprises five projects; the two largest being the closure of the Port Dundas grain whisky distillery in Glasgow and the closure of a spirit bottling plant in Kilmarnock. There is also the creation of a new bottling line in Fife.

Port Dundas Closure

Diageo’s restructuring plans envisage the Port Dundas grain whisky distillery closing in summer 2011. Diageo selected the Port Dundas site as the closure candidate because it is relatively small scale, compared to North British and Cameronbridge distilleries, which results in a cost disadvantage for every litre of spirit produced. Also significant one-off investment is required in the medium term to replace worn out assets. The company state that savings from this project will be £14 million annually based on the loss of 98 jobs in Glasgow and overheads associated with running the plant. One-off implementation costs are £14 million, the majority of which are costs associated with job losses.

Kilmarnock Closure

Diageo’s restructuring plans envisage the Kilmarnock bottling plant closing in 2011. The management’s rationale for this closure is that there is a significant level of overcapacity within the current 38 bottling line footprint at Shieldhall, Leven and Kilmarnock. Diageo’s packaging restructuring plan assumes that a new bottling hall and tank farm will be built at Leven and Kilmarnock will close. Kilmarnock was selected as the closure candidate because it is the oldest site of the three current bottling operations, is space constrained, poorly laid out for product flow and goods in/out and requires significant capital spending in the medium term to replace worn out assets. The company say that savings from this project will be £20 million annually based on the net loss of 317 jobs, overheads and maintenance capital expenditure associated with running the Kilmarnock plant. The job losses are split 82 direct jobs (line operatives) and 235 indirect jobs (support staff - e.g. maintenance/line scheduling required to operate the plant). One-off implementation costs are £120 million, the majority of which, £84 million, is associated with constructing a new bottling hall and tank farm at Leven and equipment and tooling to affect the line moves. Other costs of £36 million consist of redundancy, relocation and other costs.

Source: Scottish Government 2009d

Economic Impact

An independent assessment of the impact of Diageo's proposals has been conducted by EKOS for Scottish Enterprise and East Ayrshire Council. It estimates that the net effect of the restructuring project will be a minimum loss of 710 FTE jobs and £14m of annual GVA output. In addition, the loss of tax base, increased benefit costs and long-term health effects is estimated to cost the public sector £10,000-20,000 per job per annum – a total of £4-8 million per year (EKOS 2009).

The Economy, Energy & Tourism Committee may wish to consider how Diageo, Scottish Enterprise and the Scottish Government intend to mitigate these potential impacts.

It is worth noting that in July 2009 the Scottish Affairs Committee held two private informal meetings with trade union representatives and executives from Diageo plc to discuss Diageo’s proposals for the restructuring of its Scottish business. The Committee states that it will maintain a close interest in the future of the Kilmarnock and Port Dundas sites.
ANNEXE 2 - SUMMARY OF WHYTE & MACKAY’S RESTRUCTURING PROPOSALS

Whyte & Mackay issued a press release on 4 August 2009 indicating the commencement of a restructuring programme. It stated:

“Whyte & Mackay today announced it is undertaking a major review of its organisation which could lead to the loss of up to 85 jobs in Scotland.

Approximately 15 of the company’s sales team out with Scotland may also be affected.

The Glasgow based spirits company, which has 574 employees, has entered formal consultation for the next month to review its options and look at ways of minimising the number of compulsory redundancies.

The company has held meetings over the last week with the relevant Scottish Government ministers and officials, including the First Minister Alex Salmond.

Opposition parties, Scottish Enterprise, Scottish Development International, and Highland and Islands Enterprise have also been briefed on the situation.

Chief Executive John Beard said: “It is with regret that I have to announce this review and the planned job losses. It will come as no surprise to anybody that a combination of the world wide economic situation and the punitive UK legislative climate means that only the fittest alcoholic drink companies will survive. For Whyte & Mackay this means taking the painful decision to review our structures and costs.”

Beard added: “I can confirm that whilst this impacts all of our seven Scottish locations there will be no site closure as a consequence of this decision.

“My priority over the coming days and weeks is to help and assist our staff. We have sought the assistance of PACE (Partnership Action for Continuing Employment) to provide professional support as necessary.”

He concluded: “We are hopeful that this difficult decision will ensure Whyte & Mackay has a sustainable future going forward, leaving us in a strong position to grow when the UK and global economy improves.” (Whyte & Mackay 2009a).

Whyte & Mackay staff are spread across a number of geographical locations in Scotland:

- Glasgow headquarters: 177
- Grangemouth bottling plant: 201
- Invergordon Distillery: 133
- Fettercairn Distillery: 20
- Jura Distillery: 17
- Dalmore Distillery: 17
- Tamnavulin Distillery: 9  
  (Source: BBC 2009b)

As a result of the review around 95 people will leave Whyte & Mackay. The company are aiming to reduce the number of compulsory redundancies through offering voluntary redundancy, redeployment or relocation (Whyte & Mackay 2009b).

The Economy, Energy & Tourism Committee may wish to monitor the restructuring programme as it progresses.
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