6 A market under pressure

6.1 Market developments

The previous chapters made clear that in 2008 the production and sale of beer contributed significantly to the European economy in terms of employment, value-added and government revenues. However, we observed a number of developments in the beer market that may temper the contribution of beer to the economy in the years ahead. These main developments are:

► **Higher production prices**

There has been a significant increase in production prices in recent years. The market price of hops has risen drastically, resulting in higher costs of ingredients needed for production. These high prices are explained by disappointing hops production volumes in 2006 and 2007.[12] Production volumes in those years were not sufficient to meet brewing industry demand. The disappointing production volumes were caused by unfavourable weather conditions shortly before or during the harvest period. These higher hops prices had several consequences. Some of the breweries were forced to adjust their recipes and consumers were faced with increased prices.[13] The increased beer prices were inevitable because of the small profit margin on beer.

Besides increases in hops prices, breweries in Eastern and Central European countries were faced with significant increases in labour costs. On average gross earnings increased in 13 of the monitored Eastern and Central European countries, by 8 to 24% per year.[14] These higher wages lead to higher production costs, but another effect of the higher wages is that they lead to higher consumer expenditures. This means that consumers are able to spend more money on beer.

In most cases the increases in production prices have led to an increase in beer prices. Higher prices affect the demand for beer and may lead to lower consumption.

► **Economic downturn**

It can be expected that the current global economic slowdown will have its effect on the brewing sector. In the first half of 2009 for example, the brewers SABMiller[15] and Heineken[16] announced that consumer demand had been affected by the global economic slowdown.

To illustrate how the economic downturn can affect national markets, figures show that the market for beer in the United Kingdom suffered a 7.2% decline in the third quarter of 2008, compared to the same quarter in 2007. The fall in the fourth quarter of 2008 was 8.3% compared to the fourth quarter of 2007. The fall is the largest third-quarter decline for a decade.

12 Barth-Haas group, The Barth Report, (2007/2008).
13 Cortissoz, A., With fewer hops, prices jump, The Boston Globe, 9 January 2008.
14 Database Central Europe, Rapid increase in labour costs in Central and Eastern Europe in 2008, 19 January 2009
15 RTT News, SABMiller FY09 Profit Declines on Costs, Stronger Dollar, Update, Tradingmarkets.com, 14 May 2009.
16 Agence France Presse (AFP), Economic crisis, smoking bans hamper beer sales: Heineken, 22 April 2009.

A total of 161 million fewer pints were sold between July and September compared against the same period last year - a fall of 1.8 million pints a day (1.02 million litres). Beer sales in pubs, bars and restaurants fell in the third quarter by 8.1% and in the fourth quarter by 9.9% over the same period. Sales in supermarkets and off-licences also fell 6% from July to September compared against the same period the previous year. [17]

The accelerating decline in beer sales is a clear sign of a worsening economy, worried households and weakening spending. It is also reducing the government's revenues from duties and VAT. It is estimated that tax income for the British government from duty and VAT are down £181 million since the March Budget, compared against the same period in 2007. This is despite the fact that beer taxes went up by 18% in 2008. [18]

The likely effects of the economic downturn in terms of reductions in direct and indirect employment, and the value-added to the European economy due to beer would need further investigation.

► Changing structures of alcohol taxation

The European Commission services are currently considering the need for modernising the directive on structures of alcohol taxation (Council Directive 92/83/EEC). This directive was designed to harmonise the structures of alcohol taxation i.e. specifying the categories of product subject to excise duty arrangements, amongst other things. On the other hand Directive 92/84 laid down minimum rates for the categories of product whereby, as long as these minimum rates were met, Member States could have a degree of flexibility in setting the levels of taxation they consider appropriate to their own circumstances. Both these directives have remained largely unchanged since 1992.

As mentioned in Chapter 5, European countries differ in their levels of taxation (rate of excise), so a change in European policy will affect some countries more than others. If the EC decided to raise their minimum excise rate on beer, breweries, for example in Germany, will face higher excise rates. Breweries in the Netherlands for example, or the Nordic countries, Ireland and the United Kingdom already face higher excise rates on beer than those laid down by the EC.

The European Commission is not alone in considering the need to modernise legislation on taxes. Various Member States are also considering changing their legislation on alcohol taxation or have already changed it. On 1 January 2009 the Dutch government increased the excise rates on beer by 30%. Other countries that increased their excise rate on beer in 2009 are Estonia, Greece, Lithuania, Latvia, Hungary, Portugal, Romania, Slovakia, Finland and the United Kingdom.

As shown by our study in the Netherlands, changes in tax policy can have serious consequences for the brewing sector.[19] The supplying sectors (e.g. agriculture, transport and the packaging sector) and the hospitality and retail sector which benefit from beer production and sales will also feel the consequences of such a change in tax policy.

Moreover, there are large differences in taxation between different kinds of alcoholic beverages. Beer is much stronger taxed than for example, wine, the latter which at the time of this report (June 2009) has a zero excise rate. This will have an even larger negative effect on the consumption of beer, and on the brewing sector.

---

17 BBPA, UK Quarterly Beer Barometer, 27 January 2009.
18 BBPA, UK Quarterly Beer Barometer, 27 January 2009.
19 Increasing the Excise Duty on Beer. Penny Wise, Pound Foolish', Ernst & Young and Regioplan, Amsterdam (2008).

Increased tax burden

In the questionnaire distributed for the purposes of this study among National Brewery Associations and breweries, it was asked which taxes have been increased since our first study in 2005. The table below reinforces the perception that the tax burden on beer has changed. In most cases higher taxes lead to higher beer prices. Because of the small profit margin on beer, higher taxes are passed on to consumers. Furthermore, excises and VAT are so-called consumer taxes. These taxes are generally charged if a consumer purchases the relevant goods, in this case beer. These taxes are designed to be transferred to be charged to consumers.

Table 2: Changes in tax rates since 2005

	A slight increase	A moderate increase	A strong increase	A very strong increase
VAT	3 countries	2 countries		
Excise	3 countries	3 countries	6 countries	5 countries
Corporate taxes			1 country	1 country
Property taxes		1 country	3 countries	
Climate change levy (energy tax)		2 countries		
Vehicle excise duty		2 countries	2 countries	
Packaging taxes			2 countries	1 country
Fuel tax	1 country	3 countries	3 countries	
Other environmental taxes	1 country	1 country		

Source: 29 National Brewery Associations, situation as on June 2009. [20]

Interpreting the results of table 2 above, it can be observed that 17 countries have faced an increase in excise since 2005. Although excises are transferred to consumers, an increase in excises also affects the brewing sector. This is because the consumption of the more expensive beer in particular, comes under pressure if prices are raised.

Autonomous effects on beer consumption

There are also some autonomous effects leading to a lower beer consumption in Europe. In many countries consumers have changed their drinking habits over the 15 years. More people prefer to drink wine instead of beer. For example in the Netherlands, wine consumption per head has increased from 14.5 litres in 1990 to 21.6 in 2007.[21] In the same period the beer consumption per head has decreased from 88 to 77 litres. New generations of young people also seem to have shifted their preferences in favour of pre-mixed drinks and spirits at the cost of beer.

Another effect is that more beer is consumed at home (off-trade) instead of in the pub or other hospitality locations (on-trade).[22] This may be due to the increased prices in the hospitality sector when compared to the retail sector, but also due to other interventions (i.e. smoking bans in bars) that have led some consumers to change their consumption behaviour. The induced employment effect[23] of on-trade consumption is higher than the employment effect of off-trade consumption. This is explained by the much lower turnover per employee in the hospitality sector in comparison with the retail sector. The consequence of this switch from on-trade consumption to off-trade consumption is that fewer jobs are created because of the sale of beer.

20 The questionnaire was completed by 29 National Brewery Associations. The National Brewery Associations of Malta and Croatia did not complete this questionnaire.

21 Website of the National Statistics Office the Netherlands consulted in June 2009, http://statline.cbs.nl/statweb/.

22 Ernst & Young study on the Contribution Made by Beer to the European Economy (2009)

23 See Annex I for an explanation of the induced employment effect.

6.2 Summary of main developments in the brewing sector

The brewing sector is under pressure due to a number of developments. These main developments are:

Summary of the main developments in the brewing sector

- Higher production prices
- Economic downturn
- Uncertainty about pending tax changes
- Higher tax burden
- Changing drinking preferences at the cost of beer
- A switch from on-trade to off-trade

These developments have in common that they will affect the consumption of beer and may influence the success of the brewing sector.