



Beer Duty: maintaining momentum

A report for the Campaign for Real Ale

February 2016

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Authorship and acknowledgements

This report has been produced by Cebr, an independent economics and business research consultancy established in 1992. Cebr delivers economic analysis and forecasts to a wide array of retained private and public sector clients, and provides bespoke economic impact analysis of different policies and regulations at whole economy, sector and individual company levels.

The report was authored by Sam Alderson, Cebr Economist with supervision from Scott Corfe, Director. The views expressed herein are those of the authors only and are based upon independent research by them.

Executive Summary

Hat-trick of duty cuts has helped to revitalise the Beer Industry

- Cuts to beer duty have reversed much of the real increases in duty rates seen over the years when the Excise Duty Escalator was in place.
- Cebr previously showed the positive effects that the first two cuts in duty had on the beer industry. These included supporting higher levels of beer sales, increasing investment and saving over 1,000 public houses from closure.

However, challenges still remain

- Duty rates remain elevated when compared with both the path for duty on spirits since 1997 and to the comparable rates in other major brewing countries across Europe.
- Despite three years of cuts to beer duty, the inflation-adjusted level of duty applied to spirits has fallen by over 21% since 1997 compared with a rise of just under 3% in beer duty over the same period.
- Britons pay nearly 40% of all beer duty collected in the EU but only account for around 12% of beer consumption, highlighting the relatively high rates of duty that prevail in the UK.
- While overall beer sales had risen in the 2013/2014 financial year, annual sales of beer in the UK declined once again in 2015, down 1.5% year-on-year suggesting that there remains financial challenges facing the brewing sector.

Further cut in duty needed to support the momentum in the industry

- Cebr would argue that more could be done to build on the positive contribution of recent duty cuts and, given the substantial contribution it makes to the UK economy, truly reverse the decline of the nation's beer industry.
- According to our modelling of the alcohol model, an additional cut in duty in 2016 and subsequent freeze over the rest of the parliament would:
 - Support the sale of an additional 1.3 billion pints over the course of the current Parliament.
 - Create an additional 13,000 jobs in bars and pubs across the UK.
 - Provide an additional £75 million of investment in the brewing industry by 2020.
 - Save just under 550 public houses from closure

Review of excise duties on alcohol

Trends in the UK beer market

Economic contribution of the beer industry

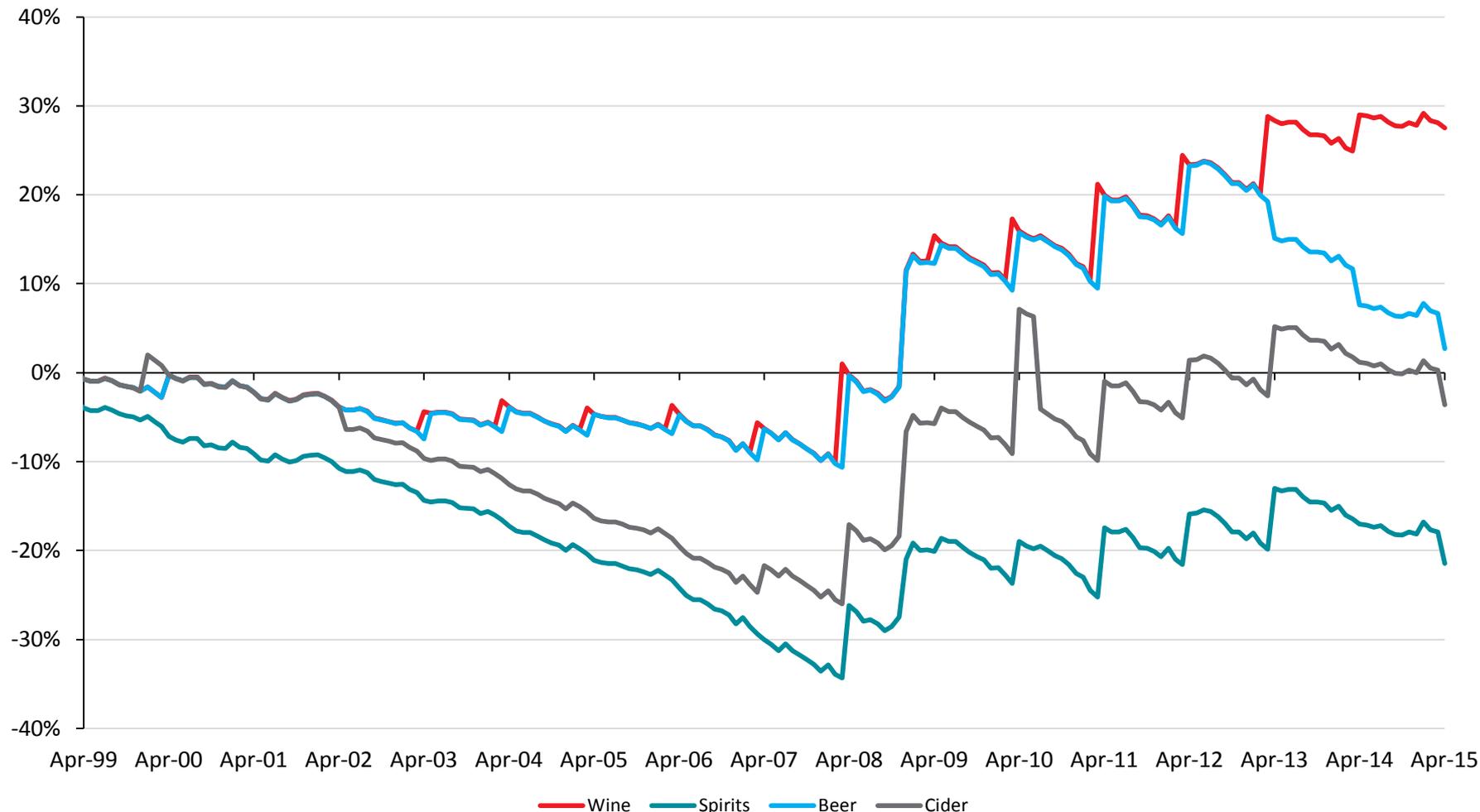
Analysis of future duty regimes

Duty Rates

- Recent history of alcohol duty rates can be split into three periods; the policies pursued between 1997 and 2007, those seen between 2007 until 2013 and the more positive measures that have been pursued in the last three years.
- Between 1997 and 2007, excise duty policy aimed to achieve 'equalisation', whereby excise duty on alcohol beverages would be directly proportional to alcohol content. As such, over the decade to 2007, beer and wine duty increased broadly in line with the retail price index (RPI), while duty on spirits remained frozen for much of the period. However, equalisation created an unfair advantage to producers of other forms of alcoholic beverages due to differences in the cost of producing a litre of pure alcohol, the cost of producing a litre of pure alcohol in the form of beer has been estimated to be around 2.4 times greater than for spirits.
- The introduction of the Alcohol Duty 'Escalator' in the 2008 budget meant that the cost of all categories of alcoholic beverage (beer, cider, spirits, wine) increased significantly faster than the general rate of price increases across the economy.
- After a well-reasoned campaign from the beer industry, the government not only officially scrapped the Duty Escalator on beer in the 2013 Budget but went further, announcing a cut of 1p in the duty placed on a pint of beer (a cut of 2%). This has been followed by two further, much welcomed cuts in beer duty in 2014 and 2015.
- However, as shown on the following slide, despite three years of cuts to beer duty, the inflation-adjusted level of duty applied to spirits has fallen by over 21% since 1997 compared with a rise of just under 3% rise in beer duty over the same period. Similarly, rates of duty on beer stand well above the comparable rates in other major European economies.

Cuts have helped to reverse the damage caused by the Beer Duty Escalator but differential with spirits still remains

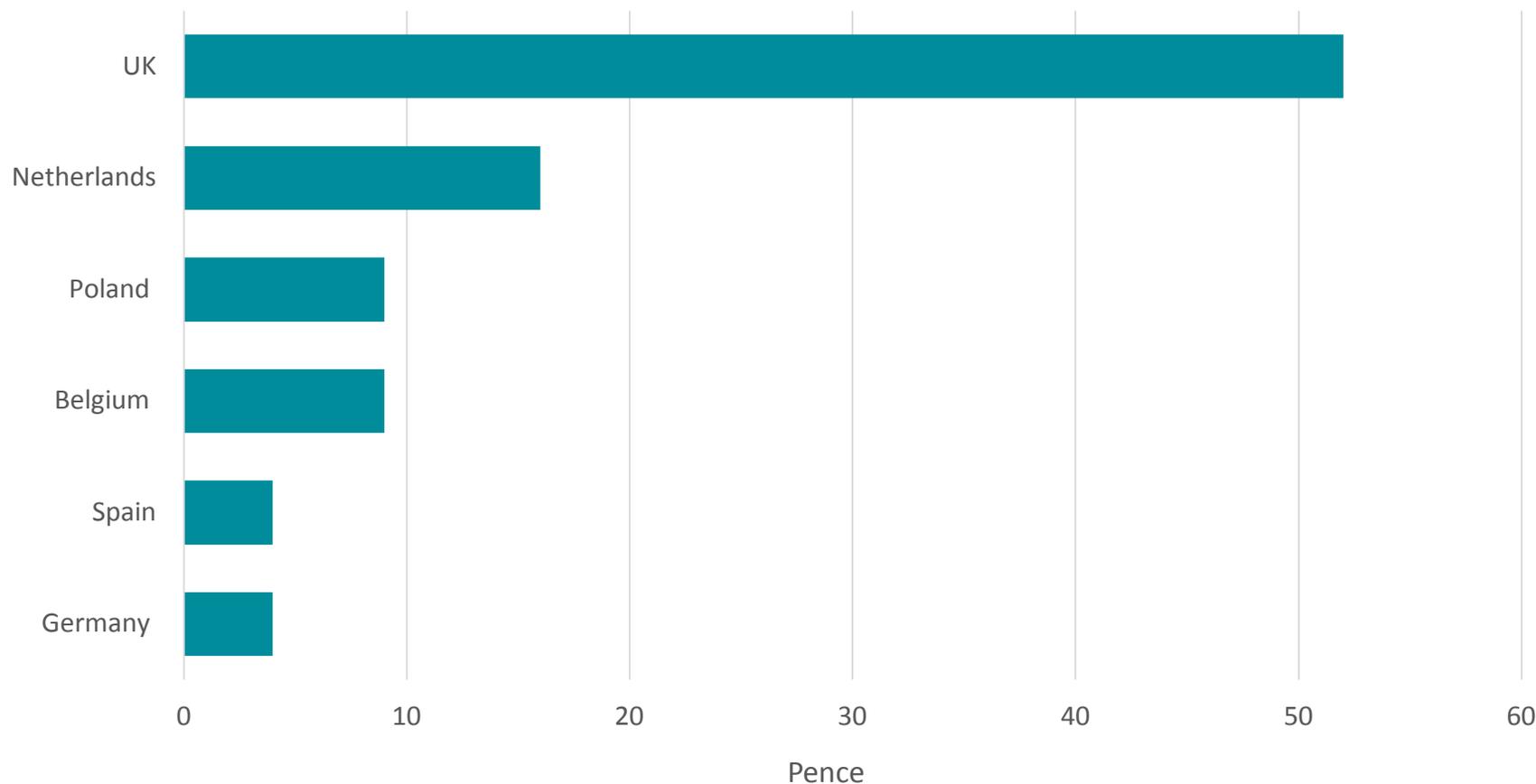
Real changes in United Kingdom alcohol excise duty since 1997 (RPI adjusted)



Source: British Beer and Pub Association, Cebr analysis

Britons pay nearly 40% of all beer duty collected in the EU but only account for around 12% of beer consumption

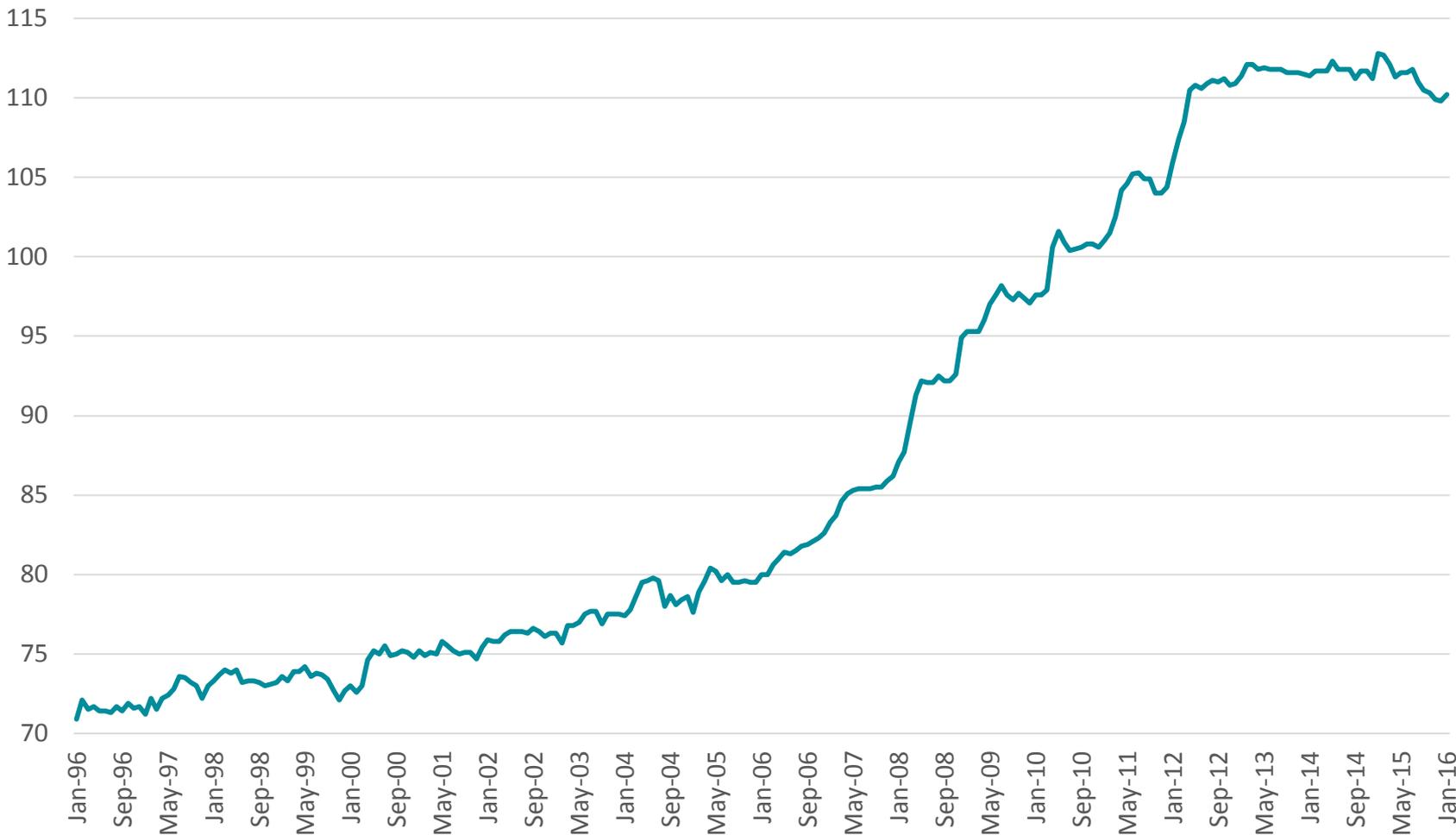
Beer duty rates in top six EU brewing nations, pence per pint of 5% ABV Beer



Source: *The Beer Story: Facts on Tap*

Duty cuts have helped keep factory gate costs steady following sharp increases in the past decade

Producer Price Index – Alcoholic Beverages inc.duty (2010 = 100)



Source: Office for National Statistics

Review of excise duties on alcohol

Trends in the UK beer market

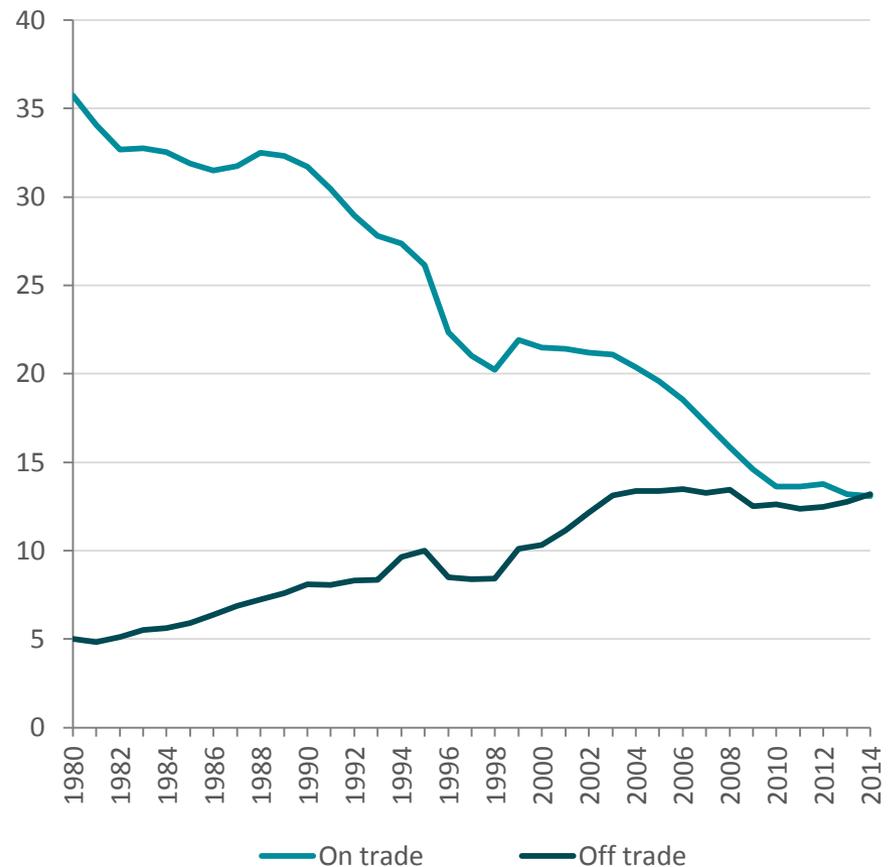
Economic contribution of the beer industry

Analysis of future duty regimes

After short-term uplift, sales of beer in the UK fell once again back in 2015

- The UK beer industry has been in structural decline since the 1980s. Over the three decades to 2013, overall consumption of beer in the UK fell by nearly a third (32.3%). In particular, there has been a significant contraction in the volume of beer consumed through the “on-trade” – which includes restaurants, hotels and pubs. The amount of beer purchased through this channel has plummeted by 60% over the three decades to 2014, now reflecting less than half of the overall market.
- However, thanks in part to recent falls in the rate of beer duty, clearances of beer increased by over 1.6% over the course of the 2013/14 financial year. However, annual sales of beer in Britain declined by 1.5% in 2015 suggesting that there remains financial challenges facing the brewing sector.
- The excise duty policies for much of the last two decades have reinforced the structural decline of the beer industry, and cannot have been the best way to raise tax revenues or protect the significant number of jobs in the beer and pub industries.
- Fortunately, the current government appears to have recognised this and its decision to cut beer duty over the past three years is a step in the right direction. In this respect, Cebr would argue that more could be done to build on the positive contribution of recent duty cuts and, given the substantial contribution it makes to the UK economy, truly reverse the decline of the nation’s beer industry.

Beer quantity released for UK consumption, million barrels



Source: British Beer and Pub Association, Cebr analysis

First two duty cuts provided a significant boost to the beer industry

- Last year, Cebr was commissioned by CAMRA to quantify the economic benefits of the scrapping of the Beer Duty Escalator and the cuts in rates in 2013 and 2014. That report found that the consecutive cuts in beer duty in 2013 and 2014 had led to:
 - An additional 750 million pints of beer purchased in the UK by the end of 2014/15 compared with a continuation of the Beer Duty Escalator.
 - Capital investment in the brewing industry being over £60 million higher in 2014 than it would have been if the beer duty escalator had been maintained.
 - More than 1,000 pubs being saved from closure.
 - Compared with the level in 2012, the policy measures of the 2013 and 2014 Budgets contributed to a total of 26,000 jobs either saved or created in 2015 that would not have been in place if the Alcohol Duty Escalator remained in place.

Insights from brewers, collected January 2015

Ant Stevens, Ledbury Real Ales

*“The removal of the Beer Duty Escalator and the reduction in the rate of beer duty by two 1p reductions has given our business the **confidence to invest in the future.**”*

*Over the past two years we have **invested in new equipment (made in the UK), made a significant investment in new casks (made locally in Hereford)** and invested in the infrastructure of our brewery itself with a **new cool room and dry store.**”*

Gary Walters, Ludlow Brewing Company

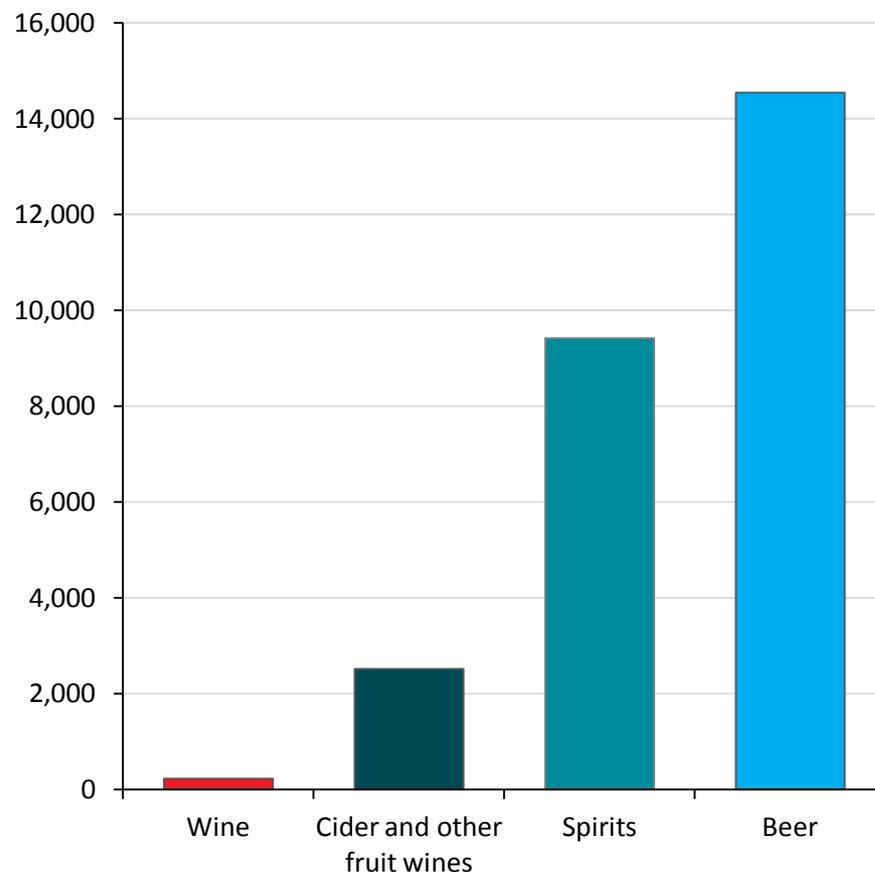
*“The cut in beer duty has given us the **confidence to put a young brewer through an apprenticeship.** The business is looking to employ **two more full time staff** within the coming months and is soon to **invest in another 3000 litre fermentation vessel.**”*

Review of excise duties on alcohol
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Beer industry remains a major contributor to UK GDP and tax revenues

- Despite the relative decline of the industry, beer production and the wider industry remain an important source of output, employment and tax revenues in the UK.
- The beer industry and the associated pub sector are estimated to contribute £22bn to UK GDP and generate around £13bn in tax revenue to the Exchequer. Further, while the industry is heavily focussed on the domestic market, the production sector, which now constitutes over 1,700 breweries, exports over 900 million pints per year to countries across the globe.
- The production and sale of beer supports employment throughout a range of industries, including agriculture, transportation and manufacturing. In total, almost 900,000 jobs are supported across the country by the activities of the brewing and pub sector.
- Beer remains the most important element of drink sales in pubs across the country. For every 10 drinks sold in a pub, on average seven are beers. As a result, it is estimated that each job in brewing supports 18 jobs in pubs.

Employment in the production of the main alcohol product categories in Great Britain, 2014



Source: British Beer and Pub Association

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Alternative duty regimes help to boost sales, employment and investment over the next four years

- This section considers the extent to which alternative alcohol excise duty regimes could be better placed to deliver on the Government's objectives of supporting UK manufacturing, the wider economy and curbing problem drinking.
- To assess whether there is a potentially superior excise duty regime to current government policy, Cebr has modelled beer sales, future tax revenues, job creation/destruction, investment and pub numbers for the following excise duty policy scenarios:
 - *Base case*: From 2015/16 onwards, duty increases by RPI inflation for all alcohol products.
 - *Scenario 1*: Beer duty is cut by a further 1p in March 2016 and then frozen at that level in the subsequent fiscal years.
- The overall conclusion from the analysis in this section is that alternatives to current plans for alcohol policy over the next few years offer better ways of supporting jobs, pubs, investment and encouraging the consumption of lower strength alcohol products such as beer. While the cuts to beer duty over the past three years have begun to support job creation in the beer and pub industries, the analysis in this report suggests that the current policy plan could threaten these boosts and further cuts to beer duty, could support more job creation and investment over the rest of the current parliament.

Modelling assumptions

For the purposes of modelling the impact of these scenarios, we assumed that alcohol excise duty increases are passed on to consumers to differing degrees, with off-trade beer duty increases seeing relatively little pass-through to consumers, and on-trade beer duty increases being passed through by more than 100%.

For on-trade and off-trade beer pass-through rates, we adopted estimates broadly in line with those made by Oxford Economics and PricewaterhouseCoopers*. Econometric analysis by these companies suggests a higher pass-through rate for on-trade beer than off-trade beer, and we have incorporated this into our central projections.

We have assumed pass-through rates of 100% for spirits, wine and cider. While there will be deviations, both up and down, amongst sellers of these products in practice, we have no evidence to suggest that, in the aggregate, pass-through rates for these other beverages are likely to deviate significantly from this norm. The full set of pass-through rates are detailed below:

Beer (on): 140% Wine: 100%
 Beer (off): 70% Cider: 100%
 Spirits: 100%

Assumptions about inflation and household income growth also need to be made, as these feed through into duty escalator calculations and also have implications for alcoholic beverage demand going forward.

Cebr Forecast (Jan 2016)	2016	2017	2018	2019	2020
Household nominal disposable incomes	4.5%	4.1%	3.8%	3.8%	3.9%
RPI (September)	1.8%	3.1%	3.4%	3.3%	3.1%

* See Oxford Economic Forecasting (2004), “Modelling the Beer Market” and PwC (October 2009), “Analysis of the impact of excise taxation on the brewing sector”.

Modelling assumptions cont.

Modelling the outlined scenarios also required assumptions about elasticities of demand for alcohol products. In the analysis which follows, we use recent HM Revenue & Customs (HMRC) estimates for alcoholic beverage elasticities of demand. Table 2 below provides an overview of the own-price and cross-price elasticities estimated by HMRC.

HMRC elasticities of demand

		On-trade					Off-trade				
		Beer	Wine	Cider	Spirit	RTD	Beer	Wine	Cider	Spirit	RTD
On trade prices	Beer	-0.77	0.54	-0.42	0.05	0.23	-0.20	0.17	0.06	-0.14	0.17
	Wine	-0.06	-0.46	-0.07	0.11	0.00	0.23	0.07	0.29	0.35	0.32
	Cider	0.16	0.09	-0.85	0.22	0.29	0.26	0.13	-0.08	0.17	0.19
	Spirit	-0.13	-0.02	-0.33	-1.15	-0.68	0.07	0.16	0.17	0.09	-0.05
	RTD	-0.05	0.24	-0.23	-0.06	-0.91	-0.04	0.16	-0.17	-0.03	-0.26
Off trade prices	Beer	-0.18	0.22	0.08	0.07	-0.14	-1.11	0.03	-0.43	-0.35	-0.30
	Wine	-0.03	0.11	-0.12	-0.10	-0.45	-0.38	-0.54	-0.91	-0.09	-0.77
	Cider	-0.04	0.30	-0.36	0.04	0.09	0.03	0.19	-1.34	0.05	-0.04
	Spirit	0.06	0.17	-0.11	-0.12	-0.11	-0.22	0.04	-0.37	-0.90	-0.51
	RTD	0.01	0.07	-0.04	0.16	-0.05	0.04	-0.05	-0.06	-0.02	-0.93
	Income	0.31	0.90	0.64	0.55	0.69	0.22	0.42	0.17	0.32	0.26

* See Oxford Economic Forecasting (2004), "Modelling the Beer Market" and PwC (October 2009), "Analysis of the impact of excise taxation on the brewing sector".

Additional 1.3 billion pints sold by 2020 as a result of a further 1p cut and subsequent duty freeze

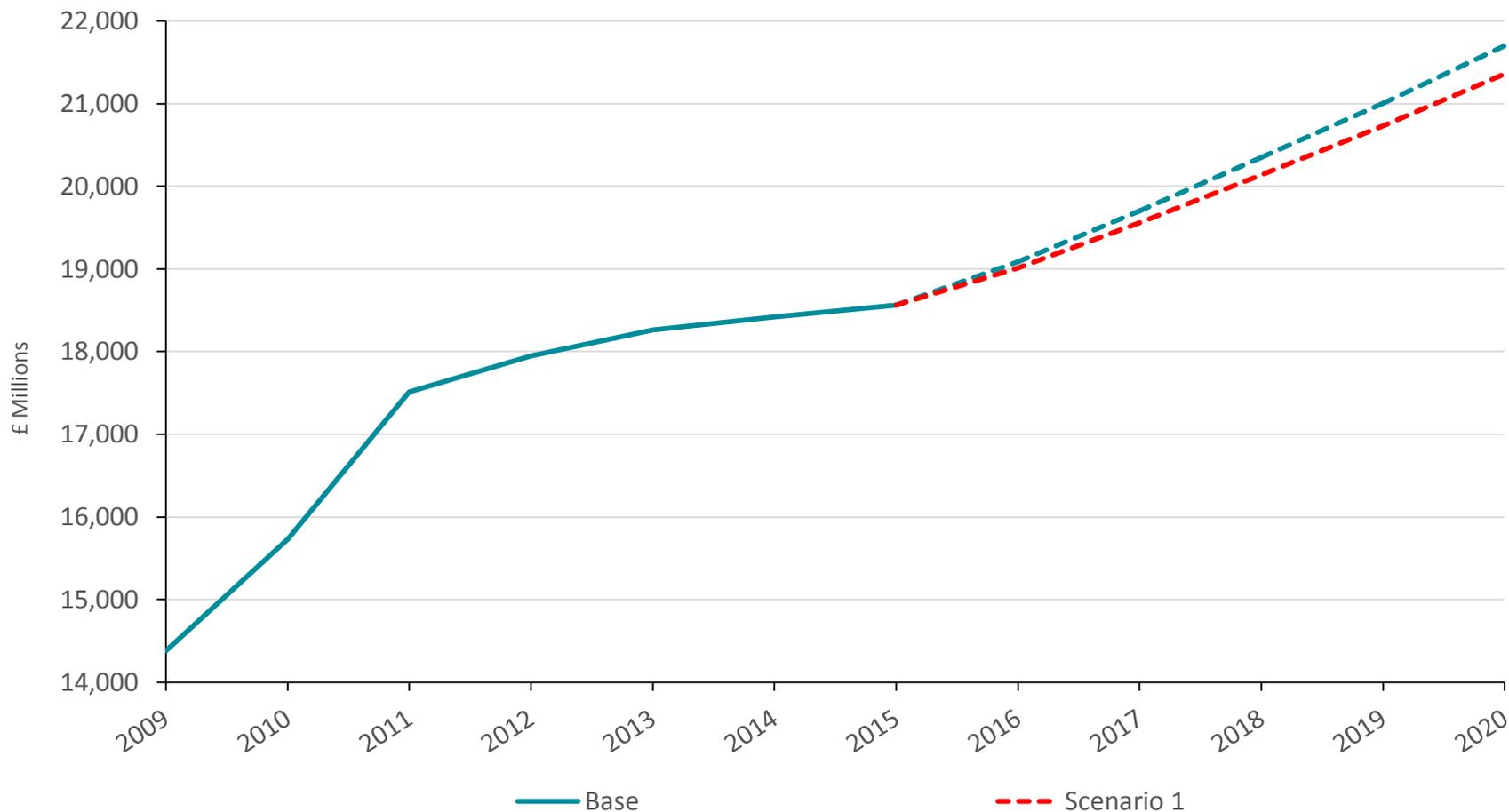
UK Beer Sales (both on-trade and off-trade), model-based estimates, thousands hectolitres



Source: British Beer and Pub Association, Cebr analysis

Fiscal impact of further cut relatively small – less than £400mil per annum by the end of the parliament

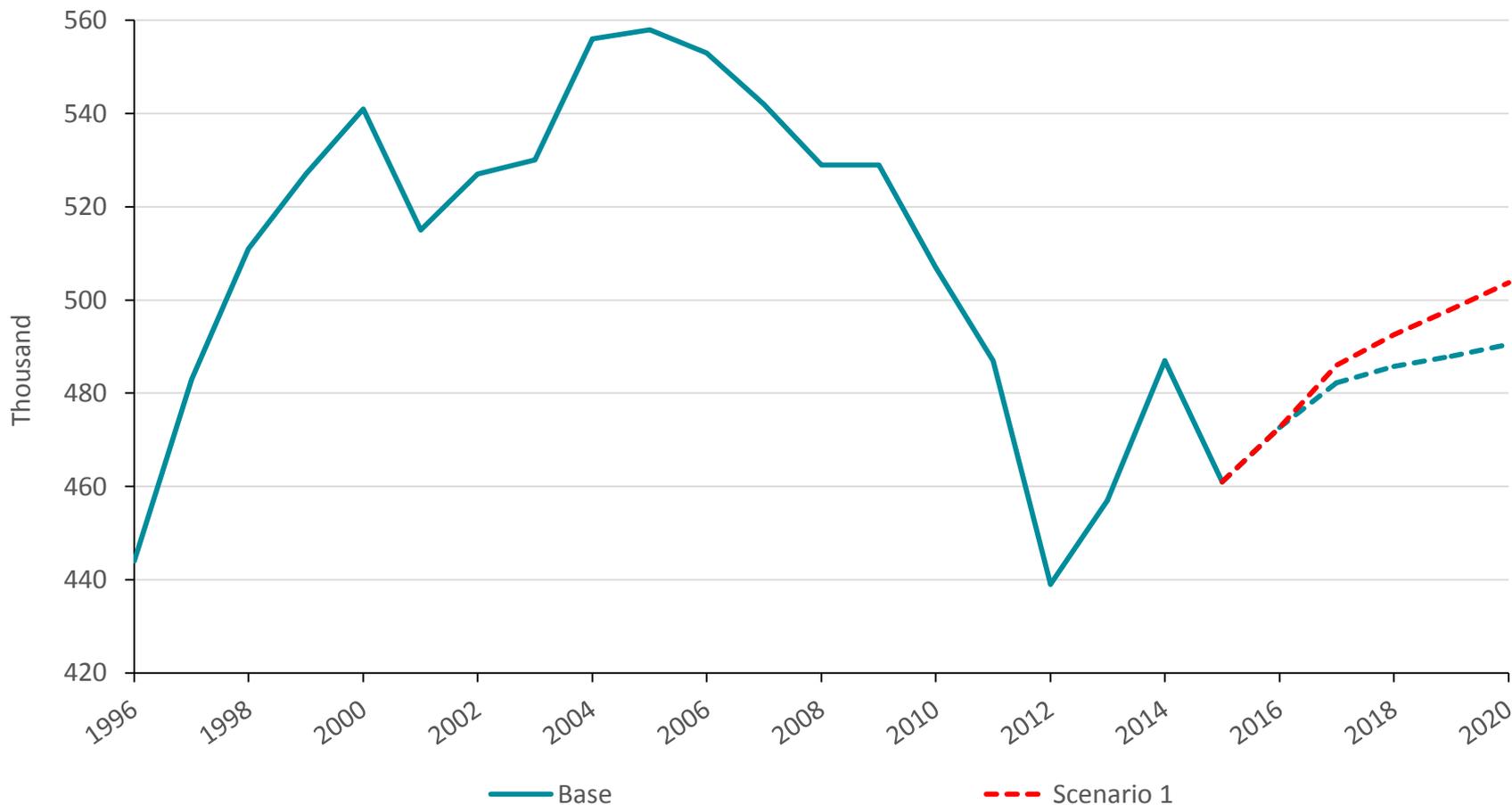
Total tax revenue from alcoholic beverages, model-based estimates, £ millions



Source: Cebr analysis

Further 13,000 jobs in bars and pubs would be created following a further cut and subsequent freeze in duty

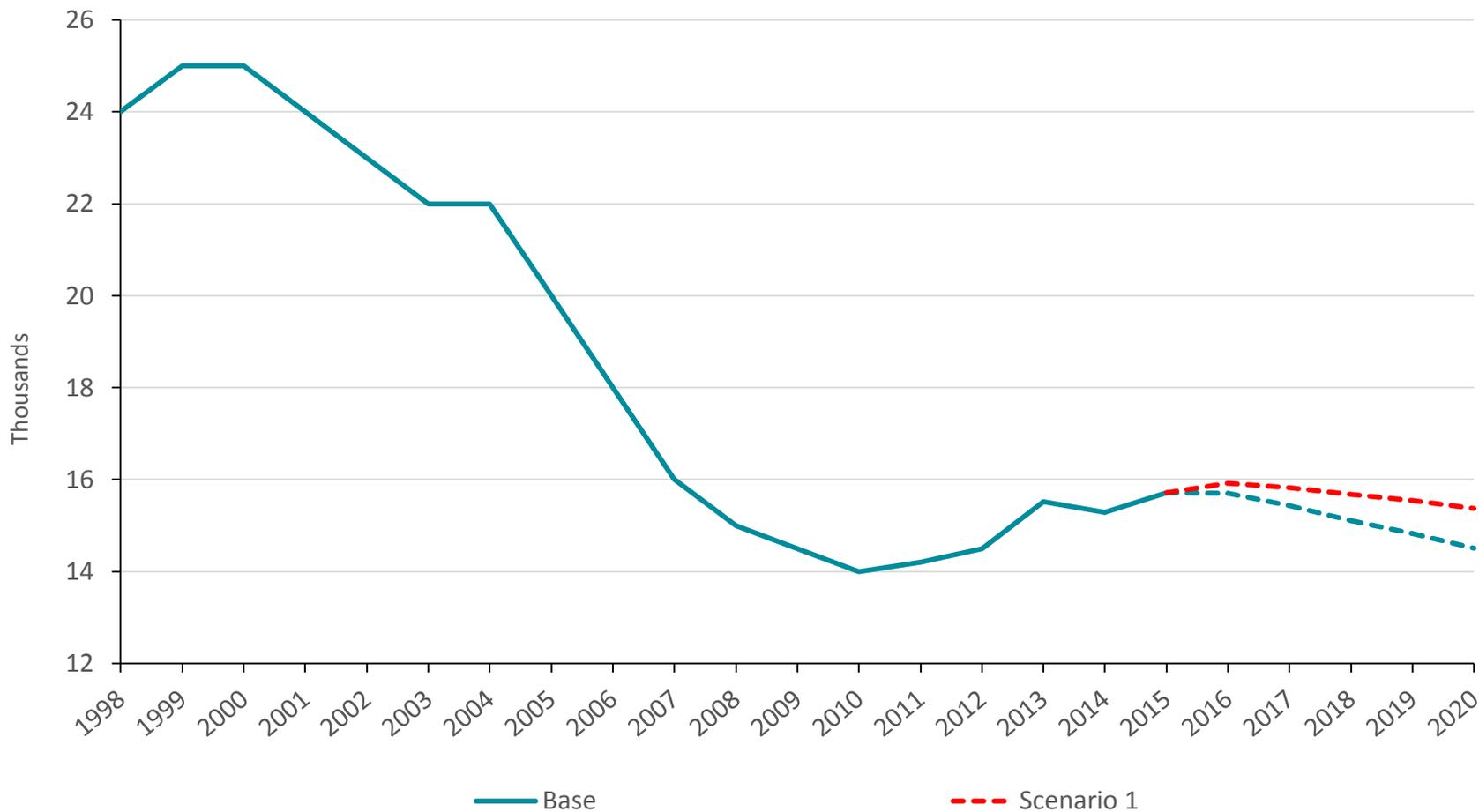
Employment in public houses and bars in Great Britain, model-based estimates



Source: British Beer and Pub Association, Cebr analysis

Further cut in duty helps to maintain levels of employment in the manufacturing of beer

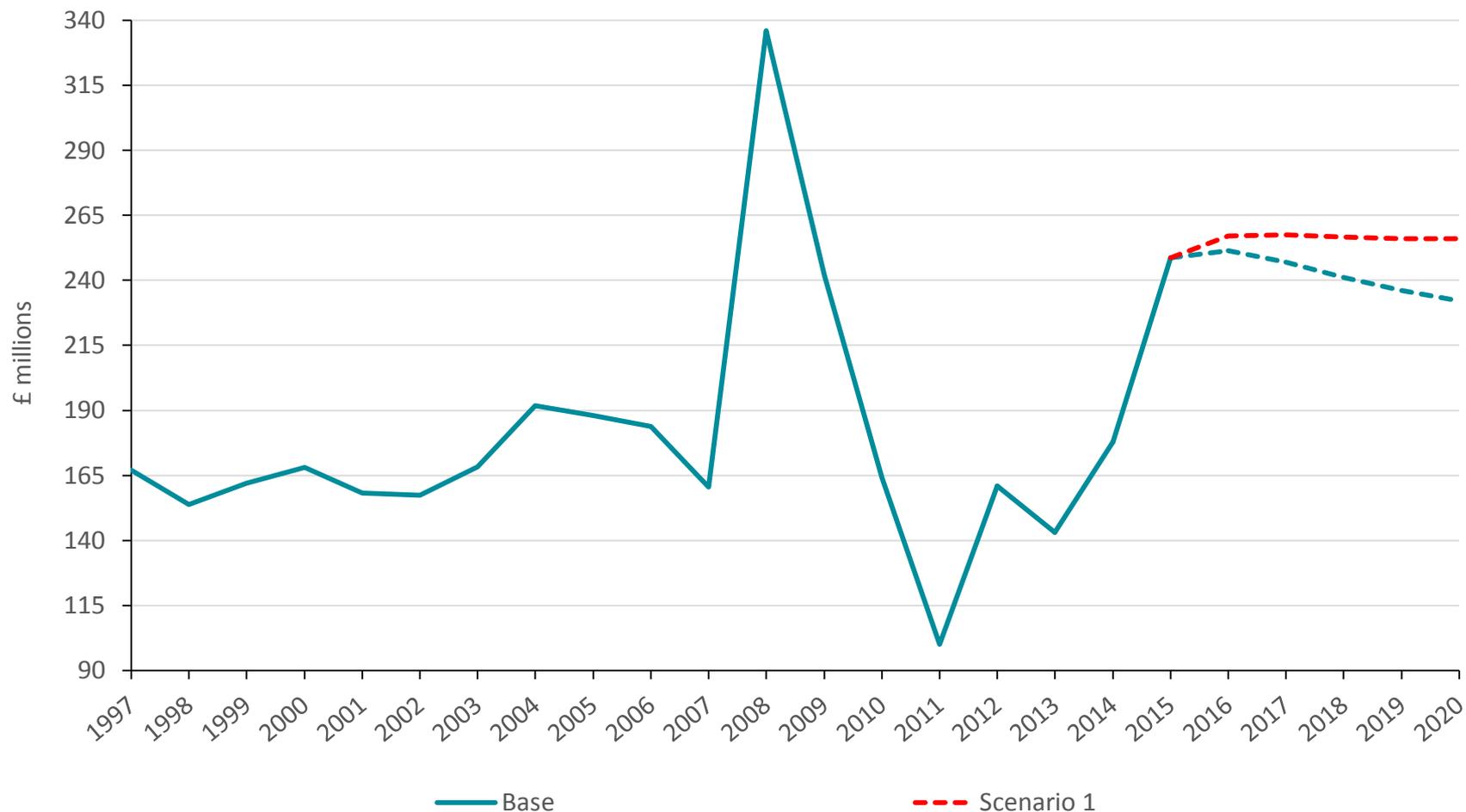
Employment in the manufacture of beer in Great Britain, model-based estimates



Source: Office for National Statistics, Cebr analysis

Boost in beer sales resulting from a further cut in duty would support more than £75 million in additional investment by 2020

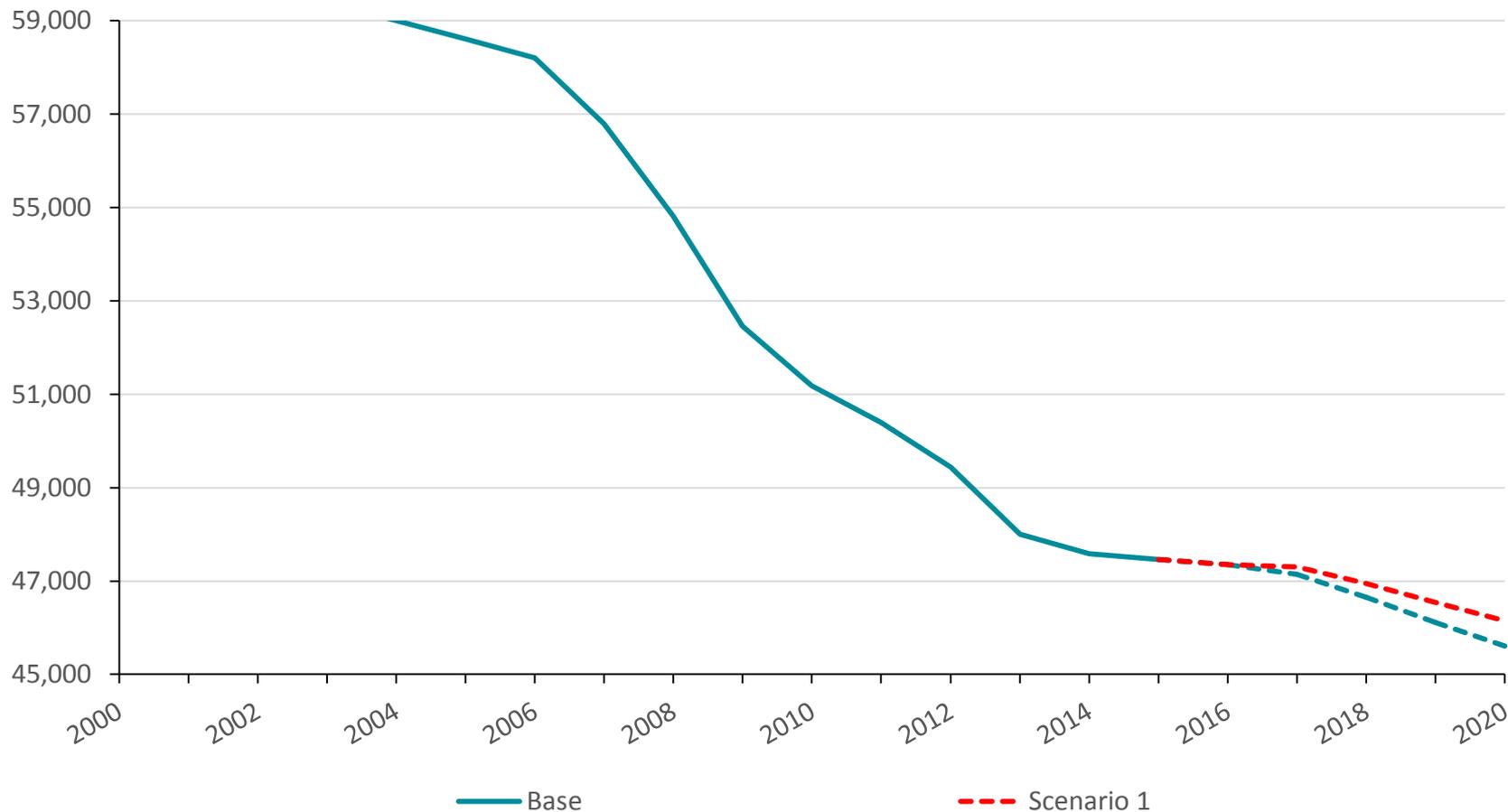
Net capital investment in the brewing industry, model-based estimates, £ millions



Source: Cebr analysis

Further cut and subsequent freeze in beer duty would help to save just under 550 pubs over the course of the parliament

Number of Public Houses in the UK, model-based estimates



Source: British Beer and Pub Association, Cebr analysis



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