



# Annual Review 2016-17

# Contents

## Page 4

Chairman's report from Pierre Pringuet, Vice President, Pernod Ricard

## Page 5

Foreword from Julie Hesketh-Laird, SWA Acting Chief Executive

## Page 7

Building strong relationships with government and informing public debate

## Page 9

Being a trusted voice in the debate on alcohol and society

## Page 11

A competitive, sustainable and fairly-taxed industry

## Page 14

Brexit: the impact

## Page 15

Protecting Scotch Whisky around the world

## Page 17

Global Affairs priorities

## Page 22

2016 Export statistics

# Chairman's Report from Pierre Pringuet, Vice President, Pernod Ricard

**The last 12 months have been a period of significant change, with the UK's vote to leave the EU a historic and seismic moment.**

The SWA has risen to the challenge, establishing itself quickly as a thought leader on Brexit related trade issues, ensuring government at all levels clearly understands the strategic importance of our industry. Whilst there will be uncertainty and challenges ahead, working closely with member companies and government, the SWA has made a valuable contribution to ensuring that the industry's voice is heard and the sector is well placed to deliver on future opportunities.

Whilst Brexit has of course taken up much of the Association team's time, there has also been the 'day job' to do. From a refresh of the Scotch Whisky Industry Environmental Strategy to a skills report, our legal protection work to the promotion of responsible attitudes to alcohol, the SWA continue to deliver for its member companies at home and overseas. And the last 12 months have also seen positive trends in the industry as exports have returned to growth, new investment has been made in the industry, and a welcome number of new distilleries have opened.

There has of course been change closer to home as well. We said farewell to our chief executive David Frost, who left us to take up an advisory role in government, and thank him for his contribution to the SWA. We look forward to welcoming his successor, Karen Betts, currently the British Ambassador to Morocco, who will join us in May 2017 after a successful career at the Foreign Office. Karen will be only the eighth head, and first permanent female chief executive, of the SWA in our 105 year history. Since David left in November,

we have also been grateful to Julie Hesketh-Laird, the acting chief executive, for her work through this transitional period.

The Scotch Whisky industry has successfully dealt with changes and unexpected world events in its long history. We always take a long term view and I have every confidence in the future. It just leaves me to thank all Council and committee members, as well as the SWA team, for their commitment, dedication and professionalism.



# Foreword from Julie Hesketh-Laird, SWA acting Chief Executive

**It has been a privilege to step-up to the role of acting chief executive, during a period of profound external change.**

Events of the past year signal further change is yet to come – not least the impact of the vote to leave the EU. Since the seismic decision in June 2016, the Association and the wider industry, along with many others, have been analysing what this means in reality. We go into more detail about the potential impact of Brexit later in this review. The continuing growth of Scotch will be a litmus test of the success of the UK's exit from the EU. While many things will change for Scotch Whisky, we are working hard to prepare for the multitude of areas where our circumstance will undoubtedly be altered.

While the Association was a proponent in favour of remaining in the EU and continuing to enjoy the benefits of the single market, we have spent time since the vote working out where opportunities in Brexit lie. And given the size and scale of our industry, it is important that governments take on board our views. Scotch Whisky is a major UK manufacturing sector supporting 40,000 jobs, adding £5bn in value across the economy and generating annual exports of more than £4bn. We have been active in calling on the government to ensure the UK has as open a trade policy as possible, protects Scotch Whisky and delivers change with the minimum of disruption.

The performance of the Scotch Whisky industry over the last 12 months has been positive and I am optimistic that this will continue.

Demand for Scotch made a welcome return to growth after a slight decline in recent years. Last year, Scotch exports were up 4% in value to more than £4bn and up 4.8% by volume to 1.2bn bottles. While Blended

Scotch Whisky continues to be the biggest category, it's also encouraging to see that Single Malt Scotch exports exceeded £1bn for the first time.

To meet this growing demand there has been substantial investment in the industry – by both new entrants and existing players. In the last three years, some 14 new distilleries have started production and around eight are set to open this year, with many more at various stages of planning and development. And companies already working in the sector have been expanding their facilities, for example with new warehouses and new and improved visitor centres.

The SWA wants to work closely with new entrants and support their growth, and the entire industry can benefit from the innovation they bring. That's why we signed a Memorandum of Understanding with the Scottish Craft Distillers Association, an organisation representing only newer, smaller producers of many types of spirits, earlier this year. The industry's expansion is largely down to the industry's desire to grow. It has been helped through support from the UK and Scottish Governments. We enjoy good relationships with both governments and we value their willingness to listen to our industry's needs, though we will continue to challenge where we see a need for change.

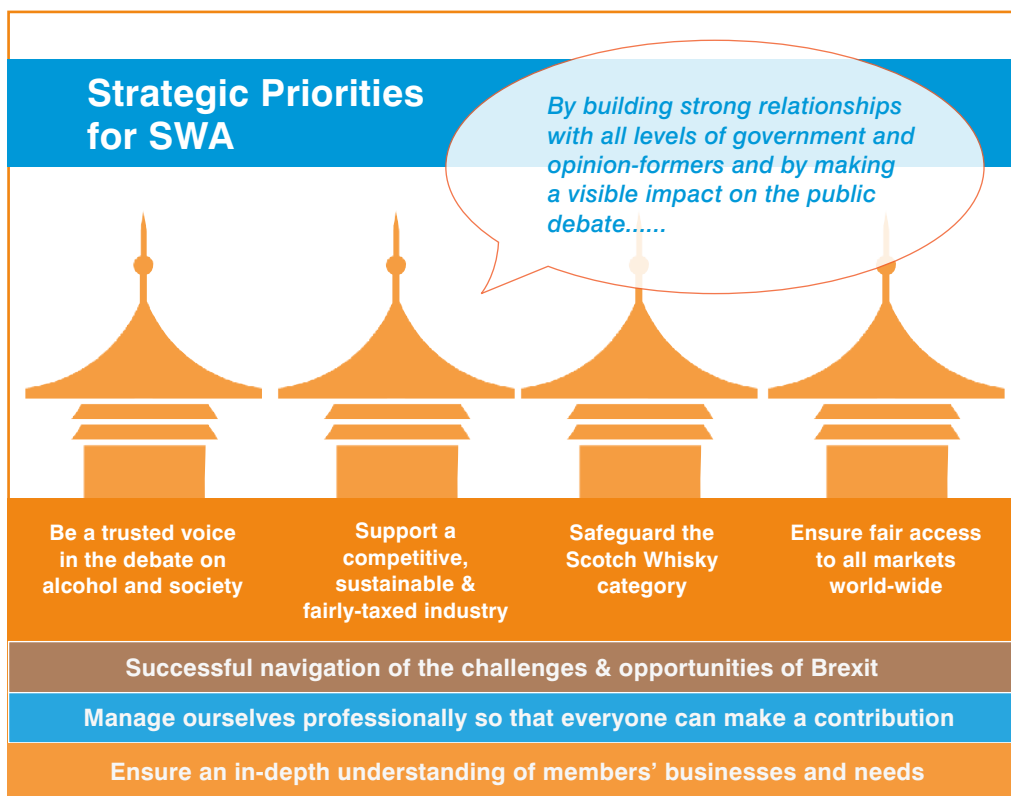
This Review gives an overview of some of the key pieces of work by the SWA in 2016 and early 2017, but it's impossible to capture all our activities in one report. From our Edinburgh headquarters and London office we will continue to represent the Scotch Whisky industry in the UK and overseas.

I look forward to Karen Betts joining as our chief executive in May to steer us through current uncertainties. I am proud to hand on a strong

Association in good shape to handle the opportunities and challenges presented by a constantly changing environment.

A strong trade association relies on the quality of input from its members and a professional in-house team. I would like to thank all our members on Council and others who support us in what we do and for our great team at the SWA for the vital role they play in our successful work.

“ Last year, Scotch exports were up 4% in value to more than £4bn and up 4.8% by volume to 1.2bn bottles. ”



# Building strong relationships with government and informing public debate

**Effective public affairs and communications underpin all the work of the SWA. We strive to advance the global interests and profile of Scotch Whisky, our member companies and the industry by engaging with the full range of industry stakeholders and all levels of government, at home and overseas.**

At UK level, our focus has been on raising awareness of the industry's priorities at home and overseas in the context of the UK's vote to leave the European Union. The SWA quickly developed a detailed analysis setting out the industry's priorities and has held meetings with ministers from new departments, the Department for Exiting the European Union (DEXEU) and the Department for International Trade (DIT), as well as ministers and officials from key departments across Whitehall. We welcomed many of these government representatives to the SWA in Edinburgh.

Following a high profile SWA campaign, excise duty was frozen in 2016, building on the historic 2% duty cut the previous year. Regrettably, that progress was reversed in March 2017 when the Chancellor increased excise duty on all alcoholic drinks by nearly 4%, adding 36p in duty to a bottle of whisky. We see that

as a major blow to a key UK sector, undermining competitiveness at a time when government should be supporting home-grown industries. As a result, the level of tax – excise and VAT – on an average priced bottle of Scotch Whisky is now nearly 80%, one of the highest levels in Europe, and 21% higher than in 2010. Looking ahead to the autumn Budget in 2017, the SWA will be arguing strongly that Brexit presents an opportunity to take a new approach to excise duty outside the constraints of EU excise law. We believe the system is in need of a fundamental review and reform to make it fair and competitive, providing a domestic platform for future growth.

The SWA has engaged with Ministers, MPs and special advisers on a range of other issues – from the Chief Medical Officers' (CMOs) alcohol guidelines to the UK government industrial strategy.

The All Party Parliamentary Group (APPG) on Scotch Whisky, for which the SWA provides the secretariat, continues to develop as an important voice for the industry at Westminster. The Group has lobbied HM Treasury for an excise duty cut, helped SWA member companies to lobby politicians on market issues in Sweden, and has visited the industry on Islay to further their understanding of the issues the industry faces.

**“Excise duty and VAT – on an average priced bottle of Scotch is now an onerous 79%, one of the highest levels in Europe, and 21% higher than in 2010.”**



UK Environment Secretary, Andrea Leadsom MP, visits Glenmorangie's bottling hall



Signing of Memorandum of Understanding with Scottish Craft Distillers Association.



Julie Hesketh-Laird (SWA Acting Chief Executive) at Dover House with Pierre Pringuet (left) and David Mundell MP, Secretary of State for Scotland.



SWA's David Williamson (right), with Scottish External Affairs Secretary, Fiona Hyslop MSP, during the US press visit

The SWA has contacts in all key Whitehall departments and good relationships with all parties in the House of Commons, ensuring the industry is rightfully seen as strategically important to the UK. At the Scottish Conservative Party conference in Glasgow earlier this year Prime Minister Theresa May in her speech to delegates described Scotch Whisky as 'a truly great Scottish and British industry'. She went on to call it 'the world's preeminent spirit'.

In Scotland, the SWA has continued to work closely with the Scottish Government on a wide range of issues. We have had successful meetings with the First Minister and Ministers relating to finance, business, energy, Europe, transport, rural affairs, environment, alcohol and health and cultural affairs. The Scottish Government also publicly supported several of the Association's initiatives including the launch of the Industry Environmental Strategy refresh and the signing of the Memorandum of Understanding with the Scottish Craft Distillers Association.

In addition, the SWA continues to provide support to the successful Scottish Parliament Cross Party Group on Scotch Whisky and regularly contributes briefings to debates and committee evidence hearings wherever there are opportunities to highlight the industry's needs and views.

Since the Scottish election in May 2016, the SWA has built new, and developed long standing, relationships with MSPs from all parties and continues to highlight the relevance and importance of the industry to Scotland as a whole.

It's been a busy time on the media front, with, as always, a regular flow of activities, to raise awareness of key issues, highlight the sector's economic importance and responding to enquiries. A lot of effort has gone into communicating the industry's position on Brexit and this has been well understood as a result. Our social media strategy and activity is being developed to build on the good work that has already taken place. We were pleased to welcome again last year a large delegation of journalists from the USA on a trip around a number of distilleries, along with our counterparts in the States the Distilled Spirits Council. This led to a lot of favourable coverage of the Scotch Whisky industry.

# Being a trusted voice in the debate on alcohol and society

**The Association collaborates closely with other trade bodies, member companies and various stakeholders to promote responsible attitudes to alcohol and tackle alcohol-related harm. In 2016 we published the fourth edition of *Matured to be Enjoyed Responsibly* which provides a snap shot of the various initiatives the industry delivered in this area.**

In 2016, seven projects received awards from the Scotch Whisky Action Fund. This makes a total of 22 awards to 20 projects across Scotland since the fund's launch in 2013. These projects reflect the fund's three themes: under 18s, families and communities. It is still early days to assess the impact of the fund as we are just starting to see the first evaluation reports coming through. We are pleased with the way the Fund is operating and there is a clear need for it as it is heavily oversubscribed. Its success is reflected in the fact the fund will have reached around 7,000 people by the end of this year.

Also within Scotland, the SWA co-ordinates the work of the Scottish Alcohol Industry Partnership. In 2016 the Partnership continued its work to promote the 125ml wine measure in the on trade and conducted a second successful pilot of the 'You're asking for it' proxy purchase campaign in Leith over the summer months to discourage adults from illegally buying alcohol for those under 18.

In October, the Court of Session ruled against the industry in the Minimum Unit Pricing case. The Association sought and was granted leave to appeal the case to the UK Supreme Court.

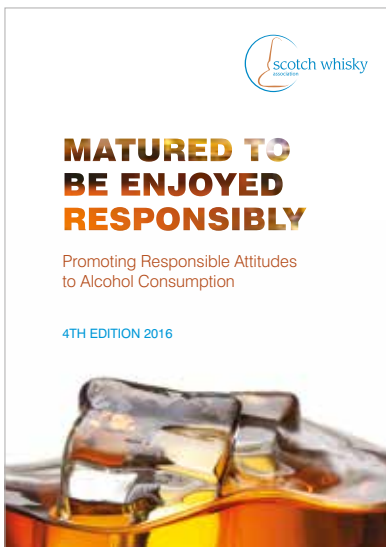
The appeal was lodged in January this year. Our application to expedite the case was accepted and dates for the hearing have been set for 24 and 25 July.

At UK level, there was the launch of the consultation last January of the UK Chief Medical Officers' (CMOs) revised low risk drinking guidelines and subsequent confirmation of the final guidelines in August, which saw some modification to the language used. Concern was expressed in particular regarding the suggestion there was 'no safe level of drinking' which was widely challenged. The industry is working with Government on guidance on how to support communication of the guidelines.

International alcohol policy remains important to the industry, given its dependence on overseas markets. We are engaging with the UK Government to argue for a balanced, holistic approach to alcohol policy in international fora such as the EU, Organisation of Economic Cooperation and Development, World Health Organisation and United Nations. We continue to play a co-ordinating role with other UK trade associations in this area. We also work closely with the International Alliance for Responsible Drinking through the Partnership Council of which we were a founding member.

New members joined the Independent Complaints Panel of the SWA's Code of Practice for Responsible Marketing of Scotch Whisky and we welcomed a new chair, Dame Anne McGuire.





“ This makes a total of 22 awards to 20 projects across Scotland since the fund’s launch in 2013. ”



Scotch Whisky Action Fund event

# A competitive, sustainable and fairly-taxed industry

**Our mission to ensure that Scotland is as competitive a place to do business as anywhere else in the UK is more important than ever given the uncertainty presented by Brexit. To ensure Scotch Whisky can compete effectively on the global stage, we will strive to help make the UK business and supply chain environment as stable and competitive as possible so the industry can grow for the benefit of all.**

## A thriving and growing industry

The publication of the UK Government Industrial Strategy is a welcome opportunity for industries such as Scotch Whisky to demonstrate how we play our part in building a successful, modern economy. It touches on a number of key areas where collaboration between the public and private sector can improve our operating environment, such as infrastructure, innovation and skills. Getting these areas right in the UK will help grow our world-leading Scotch Whisky industry.

And the industry is growing its production capacity to meet demand from around the world and many distilleries are building new warehouses. Some 14 new distilleries have opened since 2013 with many more planned. We continue to support new entrants to the industry and in February we signed a Memorandum of Understanding with the Scottish Craft Distillers Association, an organisation representing only newer, smaller producers. This is designed to encourage adoption of good practice and to facilitate the sharing of experience between established Scotch Whisky companies and new entrants.

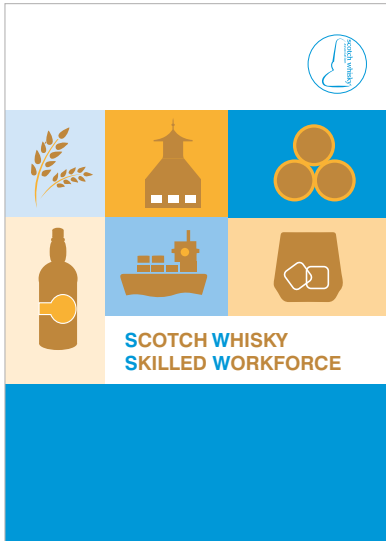
An easy to navigate regulatory environment is crucial to start-ups but also to established firms to ensure rules support rather than hinder growth. Customs, holdings and movement rules for excise goods such as alcohol



are complex. We have worked with Her Majesty's Revenue and Customs (HMRC) to drive simplification of the rules and their application and we welcome the recently announced consultation on HMRC's simplification programme. We took a prominent role in making the industry aware of its obligations under the new UK Alcohol Wholesalers Registration Scheme and helped ensure a smooth implementation of the European Union Customs Code that took effect in the spring. We are currently working with HMRC and the European Commission to make sure that the trade facilitation offered by Single Transport Contracts under the UCC continues.

## An industry that is fairly taxed

A competitive business environment at home is critical to the industry's ability to compete. Central to a competitive business environment is the tax that UK consumers pay on Scotch Whisky. After the excise freeze last year and the cut in 2015, it is therefore disappointing that the Chancellor increased spirits excise by nearly 4% in the March Budget. The tax – Vat and excise – on an average priced bottle of Scotch now stands at an onerous 79%. We are calling for a fundamental review of the excise duty system when the UK is free from the constraints of what it can do within the EU.



Casks – key part of the supply chain

When it comes to making spirits, the SWA is arguing strongly that efforts are needed to reduce the cumulative burden of taxation on businesses in Scotland. Differential taxes on businesses and employees, such as higher income tax rates, may impact on investment and attracting talent. The UK-wide Apprenticeship Levy adds to the cumulative tax burden of costs that distillers elsewhere do not pay.

The 2017 revaluation of business rates has led to distilleries in Scotland paying upwards of 7% more than those in England. We have pressed our case for fairer rates for distillers in Scotland with the Scottish Government and through the Barclay Review of Rates to ensure a fairer business environment for one of Scotland’s most important manufacturing sectors.

We were pleased that our representations on air passenger duty (APD) in Scotland have been effective and we welcome the abolition by the Scottish Government of this tax. We believe this will improve Scotland’s air connectivity and should allow new routes to open up for international business and tourist visitors.

**Looking after and developing our people**

Building on our “Scotch Whisky Skilled Workforce” publication we are working with the wider food and drink sector to help deliver Scotland’s Skills Investment Plan for Food and Drink. This articulates the skills needs facing the sector and includes an Action Plan

that focuses on four key priorities. The SWA has been nominated as Priority Champion on the group co-ordinating delivery of the ‘driving leadership and management excellence’ priority and is now working to deliver the outcomes.

The Scotch Whisky industry is one of the safest food and drink sectors for employees. The Association takes pride in our long history of supporting members’ safety and health management plans. This year our focus has been on ‘behavioural safety’, taking companies beyond compliance. We were the first signatory of the Health and Safety Food Manufacture Common Strategy Pledge that sets out our shared commitment to health and safety publicly.



**Supporting a strong supply chain**

A strong supply chain and resilient infrastructure and distribution routes are key to the Scotch Whisky industry and Scotland’s success. Distillers draw on a plentiful supply of cereals from UK farmers and merchants. To further boost collaboration between the industry and its supply chain we published a Cereals Technical Note. This will help ensure everyone from growers to grain merchants receive a clear message regarding the cereals needs of the growing Scotch Whisky industry.

And our support for the upstream supply chain received a boost early this year when the James Hutton Institute’s (JHI) proposals for an International Barley

Hub project were included in the Tay Cities Deal. This marks a significant step towards the UK Government funding the construction of a state of the art barley research facility at the JHI's base in Invergowrie.

Industry hauliers and distributors have had challenging times over the past year or so. Flooding on a main rail route south, closure of the Forth Road Bridge - a major pinch point for transport from the north - industrial action in Grangemouth and interruptions in sailings to Islay, put into sharp focus the need for a resilient and diversified transport infrastructure. In 2016 we intensified our focus on transport infrastructure in particular ensuring the industry's voice is being heard by Transport Scotland in their various consultations.

### Taking a leadership role in sustainability

Last year we furthered our sustainability ambitions in a refreshed Industry Environmental Strategy. The industry has worked collectively since the Strategy's launch in 2009 to produce and export more Scotch with fewer resources and reduced environmental impact. And it has met, and surpassed, many of its green ambitions. The strategy has been refreshed to broaden its impact and reflect an evolving world and changing business operations.

Scottish Environment Secretary Roseanna Cunningham, who took part in the Environmental Strategy refresh launch said: ***"The whisky sector has already made a significant contribution to increasing sustainability and I very much welcome this commitment to further progress. Making good whisky relies on quality ingredients and these in turn depend on our environment. It is heartening to see recognition of this in the SWA's refreshed strategy, which is an excellent example of positive interaction between our natural environment and the economy"***.

Challenges remain, especially around 'rightweighting' packaging and ensuring quality recycled packaging content. We and our industry colleagues continue to engage regularly in dialogue with our suppliers to signal the industry's sustainability ambition and requirements of them to help ensure all of the value chain can play their part. To that end we were pleased to formally lodge our support for Courtauld 2025, a voluntary commitment, to play our part in producing lower impact products more

efficiently and making the best use of our residues.

Driving increased renewable energy use in the industry is core to the Strategy as is reducing CO<sub>2</sub> and greenhouse gas emissions.



Roseanna Cunningham speaking at the Environmental Strategy refresh event

Since 2001, the Association has managed the Climate Change Agreement (CCA) with the UK Government for the whole of the UK spirits industry. CCAs, which set sector targets for energy efficiency, have been effective in delivering gains in energy efficiency and reducing greenhouse gas emissions. The review of CCA targets concluded in 2016 and we were pleased that the UK Government confirmed that the sector commitments would remain unchanged as there was limited scope for further efficiencies to be made. We were disappointed that in late 2016, it was announced that the cost of the CCA buy-out will rise from £12/tCO<sub>2</sub>e to £14/tCO<sub>2</sub>e from Target Period 3 onwards.

Further to that, the Association played a lead role in developing the food and drink sector Industrial Decarbonisation and Energy Efficiency Roadmap. The roadmap demonstrates how the whole industry can work together with public and private sector to support strong leadership, contribute to UK industrial policy as well as decarbonisation and energy supply issues.

# Brexit: the impact

**Scotch Whisky is an industry of strategic importance to Scotland and the UK. Scotch is known as a global drink. It is a major manufacturing sector supporting 40,000 jobs and adding £5 billion in value across the economy, and the single biggest net contributor to the balance of trade in goods.**

With annual exports of more than £4bn to nearly 200 countries – and the continued growth of Scotch Whisky will be a litmus test of the success of the UK’s exit from the European Union. Some things won’t change for the Scotch Whisky industry as a result of Brexit - we will, for example, still enjoy tariff-free access to the EU and certain other markets, including the USA, as a result of World Trade Organisation rules.

While Brexit creates challenges, there are also potential opportunities if the industry’s priorities are delivered.

The SWA has established good relationships with British Government Ministers and officials who lead on Brexit issues. With our members we have hosted several Cabinet level visits to industry sites across Scotland. We maximised the presence of our London office to input our into a wide range of HM government departments and consultation exercises.

We have also engaged in Brussels with spiritsEUROPE and shared our views with trade associations from the EU Member countries to find common points of agreement.

The SWA has also provided advice and views to the Scottish government. And our former CEO David Frost contributed to the First Ministers advisory panel and we have given evidence to parliamentary committees.

To support jobs and growth in the industry after Brexit, the SWA looks to the Government to pursue five objectives:

1. *As open a trade policy as possible, first securing existing EU trade deal benefits and then developing an ambitious agenda of new and refreshed Free Trade Agreements (FTAs).*
2. *Continued robust legal protection of Scotch Whisky in the UK, EU, and global markets.*
3. *Business certainty and consistency, by transposing EU single market legislation of relevance to Scotch Whisky into UK law.*
4. *Scoping out opportunities where a distinct UK approach could benefit domestic industry.*
5. *A domestic tax and regulatory agenda that delivers a platform for international growth.*

## Brexit implications for trade work

The Brexit Referendum, coupled with the Prime Minister’s announcement in January 2017 that the UK will be leaving the EU Customs Union, will require the UK to develop and implement an independent trade policy. Over the years, the legal competence to negotiate international trade agreements and take disputes in the World Trade Organisation (WTO) has largely moved from member states to EU level. While the Association is confident that the UK will rise to the challenge, the transition nevertheless represents a substantial administrative task.

The Association is unusual in having a long track record of tackling trade barriers and securing market liberalisation through engagement with multilateral and bilateral trade negotiations. It has secured successful outcomes for the industry in at least 10 separate dispute cases, one under the original General Agreement on Tariffs and Trade (GATT), eight through WTO dispute settlement, and a further one case resolved under the EU Trade Barriers Regulation. Following the Brexit vote, the Association has been sharing its expertise with government and other stakeholders and will continue to do so.



Liam Fox MP, Secretary of State for International Trade with David Frost, former SWA CEO

# Protecting Scotch Whisky around the world

## Taking effective action

One of the Association's priorities is to protect the description "Scotch Whisky" from misuse and to prevent unfair competition against the category.

We rely on members, consumers and others to report misleading products to us. While the Association often tries to resolve disputes by negotiation, litigation may be necessary. Although 15 new proceedings were authorised in 2016, we successfully resolved a number of cases.

One of our longest running court actions, against an Italian trader, finally came to an end. It began in 2001 when we were alerted by a number of UK trading standards authorities that they had received complaints from consumers who had purchased bottles of Scottish Piper and Scottish Swordsman Whisky in the mistaken belief they were Scotch Whisky. The products were made in Italy and sold to some well-known 'cash and carry' chains in the UK, Germany and Republic of Ireland.

It took 15 years through the court system, where the Association was successful at each stage and the defendant continued to appeal, before the Italian Supreme Court found in favour of the Association. Although we were confident from the outset that we had a strong case, this illustrates how a defendant can make use of the court system to delay. Fortunately, the initial raid in 2001 enabled us to stop the sale of these products quickly, even if it took us longer to obtain a final judgment.

Issues in China have again occupied a considerable amount of time. Last year we successfully concluded a civil case against one company which had been manufacturing counterfeit "Scotch Whisky" bottle caps. Due to the large scale of the operation, we decided to follow this up with a criminal complaint against the individual behind the company. With a great deal of support from both the Chinese police and the British Embassy, a prosecution was initiated in the summer of 2016 and the individual was found guilty in the first criminal case we have initiated in China, sending out a strong message that Scotch is well protected there.

Moving to the other side of the Pacific, we obtained an important ruling in Ecuador. An Ecuadorian company had been bottling and selling River House Scotch Whisky. When a sample was tested at the Scotch Whisky Research Institute, it was found to be consistent with containing unaged



neutral spirit and flavouring. The case gained some publicity when the Ecuadorian Minister of Foreign Trade referred to it in a speech as an example of Ecuador's efforts to protect geographical indications of origin.

### Objecting to misleading marks

The Association also monitors trade mark applications worldwide with a view to identifying marks which could be used misleadingly to suggest that they are Scotch Whisky. This has the advantage of identifying suspect brands at an early stage. In 2016, the Association raised objection to more than 250 trade mark applications in 57 countries. Examples of recent successes include the Association's opposition to the use of the mark Loch Ross in China and Glen Barrel in India, ensuring these marks are not registered for use on whisky which is not Scotch Whisky.

### Ensuring recognition for Scotch Whisky

In November 2016 our application to register "Scotch Whisky" as a certification trademark in Taiwan was granted. Taiwan was one of the last major Scotch Whisky markets without specific protection for Scotch. Although we had been working on our application for five years, things fell into place when we were able to show that the UK HMRC Scotch Whisky Verification Scheme guaranteed the authenticity of all Scotch sold in Taiwan whether bottled in Scotland or locally.

Now that Scotch Whisky receives recognition in most of its major markets, the Association is working to ensure it obtains legal recognition where opportunities present in smaller markets. Mozambique recognised Scotch Whisky as a Geographical Indication last year and both the

Republic of Iraq and Iraqi Kurdistan granted Scotch Whisky certification trade mark status, a first for a spirit in that region.

### Advising on compliance

Another pillar of our work involves providing an opinion on the application of the law in areas of interest to Scotch Whisky producers and brand owners. For example, the UK Scotch Whisky Regulations 2009 and the EU Technical File for Scotch Whisky set out a number of labelling rules for Scotch Whisky which ensure that, among other things, consumers are clear as to the nature and origin of the product. These rules apply high quality standards not found in the rules for whiskies of other origins. In the course of 2016, the Association provided an opinion on request, and in confidence, for around 300 draft labels.

### A world of change

The political landscape is fast moving, following the UK's decision to leave the EU. The industry places great value in Scotch Whisky's international reputation and legal recognition as a product which must be produced in Scotland according to traditional practice. The Association will continue with its efforts to ensure that there is robust legal protection of Scotch Whisky in the UK, EU and in global markets. You can read more about the potential impact of Brexit on Scotch Whisky elsewhere in this Review.

# Global Affairs priorities

**Scotch is exported all over the world and loved by millions of people. But shipments of Scotch do not always have an easy passage into global markets. Trade barriers can be financial, in the forms of tariffs, taxes and other levies, or they can be more practical such as labelling rules or customs processes. The SWA has to narrow the focus of where it tackles issues that matter most to its members and where it is able to make a difference.**

This part of the Annual Review gives a flavour of that activity by the SWA to ease the distribution of Scotch around the world.

## Geographical Priorities

### TOP PRIORITIES

**INDIA:** The Indian market continued to perform strongly, with direct exports alone up 18% in volume and 14% in value, moving India into the industry's top 10 export markets by value for the first time. A contributor to that growth was exports of bulk Scotch Whisky for use in local 'Indian Made Foreign Liquor' (IMFL), demonstrating once again that both local and imported players in the market have a common interest in liberalisation of India's exorbitant 150% Basic Customs Duty (BCD). The most likely driver for reduction in the BCD, following Brexit, appears to be a UK/India free trade agreement (FTA) negotiation. The Prime Minister and the Secretaries of State for International Trade and Foreign Affairs raised this with Indian counterparts with SWA support. The Association is working with the UK government to ensure that Scotch Whisky is at the forefront of Ministers' thinking in 2017.

The industry successfully negotiated various problematic issues in 2016, notably the implications of new legal metrology rules for labelling and beverage alcohol being excluded from the ambit of the new Goods & Services Tax. Meanwhile, the 'demonetisation' initiative, introduced at short notice in November, had a short-term impact across the consumer goods sector given the lack of banknotes in a predominantly cash-based society.

**COLOMBIA:** The discriminatory excise tax and anti-competitive monopoly practices led to a WTO panel being formed in September 2016. Subsequently, Colombia passed a new alcohol bill in December 2016 with the aim of eradicating the discriminatory measures. While this is a welcome move by Colombia, the industry is currently in the process of analysing the impact of the new Bill. We will continue to monitor how the provisions of the Bill are being implemented in practice in 2017. Direct exports rose 14% to £26.6 million in 2016 showing the potential of the market.



Left: SWA meets officials in China. Middle: Signing in Brazil. Right: SWA's Sarah Dickson, SWA global affairs director



### HIGH PRIORITIES

**THAILAND:** Thailand's restrictive approach to alcohol regulation continues, albeit there were no significant changes introduced in 2017. Nevertheless, the market fell 14% in 2016, with direct exports accounting for a shipment value of £34m. Towards the end of the year, a reform of Thailand's tax regime concluded with a revised framework for beverage alcohol taxation. This appeared likely to continue the gradual move towards specific taxation seen in recent years, a rationalisation of the number of retail licenses and a change in the taxable base of the ad valorem element of the excise tax from 'last wholesale price' to 'suggested retail price'. While the overall direction of travel appears to be in a positive direction, concerns remain about how the new system will work in practice. In addition, the Association remains disappointed that little meaningful progress was made towards addressing the longstanding issue of Thailand's WTO-incompatible tax discrimination in favour of local white spirits. Nonetheless, the details will be set in implementing secondary legislation in 2017, with entry into force likely in the second half of the year.

**CHINA:** Direct exports to China edged up 1% to £41m in shipment value in 2016, bringing the decline of recent years to a halt. The proposal by China to require imported goods to be accompanied by certification issued by their home governments is a cause of concern and the Association was able to discuss this directly with Chinese officials in Beijing in November. With effect from October 2017, Scotch Whisky imported into China will have to be accompanied by UK government certification confirming that the product complies with Chinese standards. While supporting the objective of consumer protection, the Association recognises that it is not appropriate for the UK to certify that goods comply with Chinese standards. We are working with the European Commission, UK Government and others to deliver an alternative that will satisfy the Chinese government while avoiding additional burden on the industry.

**BRAZIL:** A market visit to Brazil in November 2016 led to the successful signing of a Cooperation Agreement between the SWA and the Association representing the Cachaça industry, IBRAC in December. The two Associations have agreed to work together on areas of mutual interest

and share best practice. Through our recently refreshed network of contacts in the market, we continue to encourage fairer taxation for Scotch Whisky, an exemption from allergen labelling and protection for Scotch Whisky as a Geographical Indication.

**SWEDEN:** The Association is committed to reducing climate impact and in this context raised serious concerns about the effectiveness of the Swedish alcohol retail monopoly Systembolaget's plans to introduce a 'heavy bottle fee' to tackle this issue. In a welcome move and as a consequence of an intense industry dialogue with the monopoly, the latter has postponed the introduction of the measure, now to 2018. Meanwhile the SWA's interaction with the monopoly continues at various levels to explore alternatives. An invitation to meet with the Association in Scotland and to learn about the industry's environmental strategy and companies' concrete sustainability measures was accepted by Systembolaget and took place in Spring 2017.

**SOUTH AFRICA:** South Africa is Scotch Whisky's largest market in Africa and the Association and its member companies held a successful meeting in Johannesburg in July

2016. Even though the burden of the 10% tax rebate on pot still brandy and the threat of health warnings appear to have abated, the industry continues to engage with South African and UK stakeholders to see how the National Liquor Policy Proposal develops, following our submission of comments in November 2016. We have also been discussing with local industry a new issue, namely the misalignment between South African and UK law as to how Blended Malt Whisky is defined.

**TURKEY:** 2016 was a difficult year for Turkey, overshadowed by terror attacks, the attempted coup in July and the refugee crisis. The political and economic situation has been impacted by these challenges and the outcome of the referendum in April 2017 will be key for the future of the country. Business is suffering from the volatility of the political climate and the security situation and the impact this has on tourism. Industry efforts to improve market access continue nonetheless and concerns about trade barriers are being raised in relevant fora, including the forthcoming negotiations about the modernisation of the EU-Turkey Customs Union. As a welcome result of the Association hosting a Turkish delegation to Scotland in May 2016 to discuss the detail of product testing with the relevant experts from HMRC and others, frequency of analysis for Scotch Whisky was reduced by half. We are following up with the Agriculture Ministry to ensure this reduction is applied consistently.

**MEDIUM PRIORITIES**

**ASEAN:** After Thailand, Vietnam

was again the principal focus for the Association in the ASEAN region. The Association took part in high level meetings with Vietnamese government Ministers, including the Prime Minister, during EU Agriculture Commissioner Phil Hogan’s visit in early November. Further progress was made on market access issues, notable licensing, during the year. However, the Association remains concerned that the reform of the Special Consumption Tax, which entered into force in January, will negate the improvements flowing from tariff elimination under the EU/Vietnam FTA, as highlighted by the Commissioner during his visit.

Meanwhile, the Association is laying the groundwork for the opening up of the Burma market to imported spirits. Work is underway in the region to secure common ground with the local industry in order to facilitate this.

**MEXICO:** Direct exports rose slightly in 2016 in volume terms (1.2%) but were down by value (3%) on the previous year to £111.5m. The SWA has continued to encourage Mexico to introduce an appropriate definition

for Whisky under its draft standard on the definition of alcoholic beverages. While not yet published, Mexican officials appear supportive of our suggested changes to date.

**SERBIA:** The Association visited Serbia in November 2016 and met with various Government representatives to consider the situation for Scotch Whisky exports to Serbia. With the Serbian Finance Ministry we raised our key concern - the longstanding tax discrimination against Scotch Whisky – to explore what progress could be made. Separately, the Commission and UK Government continue to urge Serbia to remove the discrimination, which is in breach of the country’s obligations under the Stabilisation and Association Agreement.

**ANGOLA:** Sadly, exports to Angola suffered greatly in 2016, as the government kept in place both the restrictions on forex access introduced by the Central Bank in 2016, and the tax discrimination between local and imported goods, brought in in 2015. We are working with the UK in London and Luanda



ITIC tax dialogue in Cape Town

## Free Trade Agreements when the UK leaves the EU

When the UK leaves the EU, UK exporters will cease to benefit from the preferential access afforded by implemented EU FTAs. A key request that the Association continues to make of government is that this preferential market access is retained post-Brexit. The mechanisms used to retain UK access might vary from market to market. It is possible that transitional arrangements might be made in some cases in order to pave the way for a formal negotiation. There are, in fact, a relatively small number of markets where the industry would see increased tariffs in the absence of a bilateral agreement, notably Korea and Vietnam (albeit the latter is not yet in force), so we would hope solutions can be found. The Association will continue to press the industry's case, as the UK's leading contributor to the balance of trade in goods.

Any trade negotiation is a complex web of trade-offs. The mere fact that the UK is instinctively favourable to trade liberalisation and may have fewer 'defensive' interests than the EU could lead to the conclusion of rapid, ambitious UK bilateral FTAs, but the two are unlikely to correlate exactly. The Association will continue to work with government to identify priority markets and issues within those markets in support of future UK trade policy.

to find ways forward on both issues in a challenging environment. External factors like Angola's balance of payments will continue to affect its policy towards importers. Nonetheless, any new policies should be introduced in a WTO-compliant manner.

**TAIWAN:** Taiwan is the industry's fourth largest export market by value overall, with exports in 2016 worth £175m in shipment value, despite a slight fall over 2015. The success of Single Malt Scotch Whisky, in particular, is driven by sophisticated consumers and a mature regulatory environment. In the absence of significant market access issues, the Association will continue to monitor the market closely, but has taken Taiwan off its list of medium priorities.

### CROSS CUTTING ISSUES

**EU Free Trade Agreements:** Despite some last minute hurdles, 2016 saw progress towards the ratification of the agreement with Canada – CETA – now likely in March 2017, with EU/Vietnam also on the

ratification path. There were signs of hope that negotiations between the EU and Japan had picked up momentum, while the Commission began talks with the Philippines and Indonesia. Less positively, although efforts were made to revive the long stalled EU/India FTA negotiations, these did not prove successful, while political issues continued to block the EU/Thailand talks.

**Public Health:** Examples of the global affairs team work to support the international aspects of SWA's social aspects strategy and ensure effective legislation on public health issues are numerous. To name one, we worked closely with the Irish Spirits Association and spiritsEUROPE on the draft Irish Public Health (Alcohol) Bill, which is still subject to debate in the national parliamentary process. Ireland has not responded to the 10 Detailed Opinions and five comments issued by member states and the Commission under the TRIS procedure. These highlighted concerns about various provisions in the draft bill, such as Minimum Unit Pricing, onerous labelling provisions,

advertising and retail restrictions.

### Definitions and GI registration:

Work on GI protection and quality definition for Scotch and the wider whisky category continues around the globe. We submitted comments on whisky definitions in places as diverse as Mexico, Nepal and East Africa.

### WTO/Trade Facilitation

**Agreement:** The implementation of the Trade Facilitation Agreement (TFA), agreed at the WTO Ministerial Conference in Bali at the end of 2013, requires ratification by two thirds of WTO Members before it can come into force. This is likely to have been achieved by summer 2017. The TFA is intended to simplify and streamline Customs and other formalities relating to moving goods across borders. The TFA also promotes the automation of Customs procedures to avoid excess paper work and minimise opportunities for corruption. WTO studies suggest that its implementation will generate economic benefits well in excess of the combined value of all tariffs applied to goods

worldwide, with improvements being particularly marked in developing and least developed country markets. The TFA recognises that it will take time and investment for many countries to deliver the necessary change. This will not happen overnight. However, it has delivered a structure within which governments have indicated what they need to do to comply and where support from international institutions, such as the World Bank, and technical assistance from other stakeholders, including industry, is required.

**Tax:** Tax issues continue to be a major focus of our work. In addition to the geographical tax work outlined earlier, the SWA has undertaken regional work such as a speaking role at the ITIC Africa tax dialogue in Cape Town in 2016. We also monitor tax changes across the world. One such example is our work on discriminatory taxes within the EU where infringement proceedings are at various stages on the small distillers’ derogation in Croatia, the discriminatory health tax in Hungary and the illegal tax preferences for tsipouro and tsikoudia in Greece. Separately, the Association uses the mid-term review in 2017 for the FOD rum derogation in France to challenge the measure and make the case for the removal, or at least phasing out, of the spirits’ preferential treatment.

**EU Regulation:** Since the UK’s EU referendum, the team has focused on ensuring EU single market legislation with implications for the industry can be brought into UK law without any problems. Putting Brexit to one side, we are looking at changes to

existing EU legislation that will affect Scotch Whisky producers for many years to come, above all with the EU Spirit Drinks Regulation. The European Commission released a proposal to update this Regulation in December 2016. With our colleagues in Legal Affairs, we successfully worked with the European Commission to ensure that proposals on the Geographical Indication (GI) parts of the Regulation reflected the best protection possible. We are now working hard with member companies, Defra and MEPs on a series of technical matters to ensure the rules continue to protect the interests of the Scotch Whisky industry.

**Labelling:** Earlier this year, the European Commission finally published a long anticipated report looking into nutrition and ingredient listing rules for alcoholic beverages. Our priority is to ensure that any future rules in this area contain sufficient flexibility for producers to provide calorie information in a format that is simple to understand and linked with actual serving size, supporting consumer choice.



**Glass (25ml) of Scotch Whisky 40% abv**  
55 Calories  
1.0 UK Units



**Pint (568ml) of beer 4.0% abv**  
182 Calories  
2.3 UK Units



**Bottle (330ml) of beer 5.0% abv**  
142 Calories  
1.6 UK Units



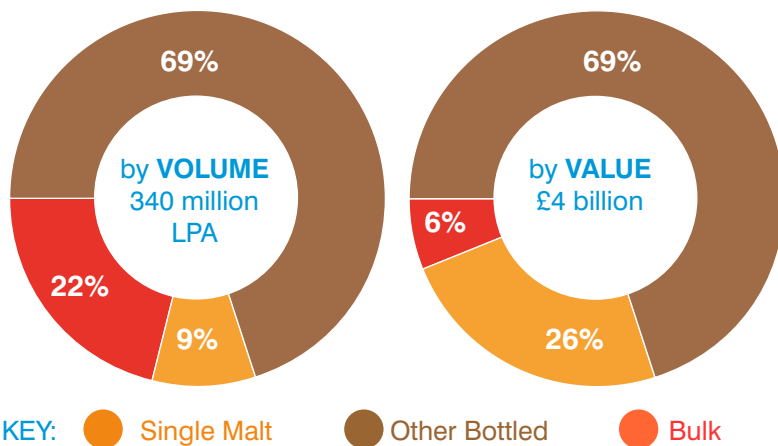
**Glass (175ml) of wine 12.0% abv**  
130 Calories  
2.1 UK Units

# 2016 Export Statistics

The value of Scotch exports increased 4% year on year to exceed **£4 billion** in 2016.




## EXPORTS OF SCOTCH WHISKY IN 2016



## QUICK FACTS...

Total exports are equivalent to:

 More than **1 billion** bottles of Scotch Whisky

Almost **39** bottles exported every second 

 **£127** every second

In 2016, Scotch Whisky was exported from the UK directly to **182 countries**, a clear sign of the global nature of the industry.

While exported directly to so many countries, **78% of exports were delivered to the top 20 markets** as a first port of call. However, despite this concentration within the major markets, several are used as international hubs where Scotch will be forwarded to other parts of the region, further extending its global reach.

An additional **56 million bottles of Scotch whisky were exported in 2016** of which 24 million were bottled Blended Scotch. Single Malt exports increased by over 10 million bottles to more than 113 million bottles and the value of Single Malt exports surpassed £1 billion for the first time.

The **EU maintained its position as the main region for Scotch Whisky exports** accounting for £1.2bn or around a third of the value all Scotch exports.

**North America** provided strong support for Scotch Whisky exports in 2016. It was the second biggest market by value with **exports reaching £1bn**.

Asia is the third largest region in value, **worth almost £786m in value**.



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