SCOTCH WHISKY ASSOCIATION

BUDGET SUBMISSION

JANUARY 2021

CONTENTS

MEETING THE COVID CHALLENGE

The Covid-19 pandemic will shape the 2021 UK spring budget.

The pandemic has already caused devastating loss of life in the UK and around the world. It continues to seriously impact the daily lives of everyone across the UK. And it has presented unprecedented challenges to the economy.

For the Scotch Whisky industry, Covid-19 represents the most difficult trading environment for a generation. In the UK and across export markets, consumer confidence has declined, hospitality has been hit hard, and the reduction in international aviation has all but ended global travel retail.

The decisions the Chancellor will make on 3 March 2021 are critical for the industry - and for the UK's economic recovery. The choice is clear - the budget can make the industry **a partner in recovery**, helping to support over 40,000 jobs across the UK, boosting investment in areas of low-economic opportunity, and back a return to growth at home and abroad. Alternatively, the industry can be left to deal with the impact of Covid-19 in 180 global markets without the firm footing of fair tax treatment in the UK, all the while suffering half a billion pounds in lost exports due to tariffs in the United States.

In our 2021 Budget Submission, we set out three ways the Chancellor can make the right choice and back growth, investment and opportunity.

First, cut spirits duty. Spirits are taxed more per unit of alcohol than beer, cider or wine. 70% of the average priced bottle of Scotch is collected in duty and VAT. This is significantly holding the industry back. Recent modelling suggests that a cut of up to 5% will grow government revenue by almost £750m over the next three years compared to the built-in inflationary increase.

Second, now the UK has left the EU, commit to reform alcohol taxation by Autumn 2021. The Queen's Speech committed to a review "to ensure our tax system is supporting Scottish whisky and gin producers." Now is the time to back domestic producers of alcohol, and ensure Scotch Whisky and other spirits are not put at any further competitive disadvantage.

Third, back a green recovery by further investment in net-zero projects in the distilling sector, including for the use of hydrogen and high temperature heat pumps. Building on the £10m fund announced in March to help distilleries go green, further government support in our environmental future will help us to overcome present economic challenges.

The Scotch Whisky industry stands ready to help the economy build back better. **Lift the nation's spirits - cut duty.**

"The government should seriously examine the potential for a cut in spirits duty."

Centre for Policy Studies; Feb 2020

3 WAYS TO BACK GROWTH, INVESTMENT, & OPPORTUNITY ON 3 MARCH '21

CUT SPIRITS DUTY TO BOOST REVENUE & CONSUMER CONFIDENCE

COMMIT TO REFORM ALCOHOL TAXATION BY AUTUMN 2021

INVEST IN ACHIEVING OUR NET-ZERO AMBITIONS

A PARTNER IN RECOVERY

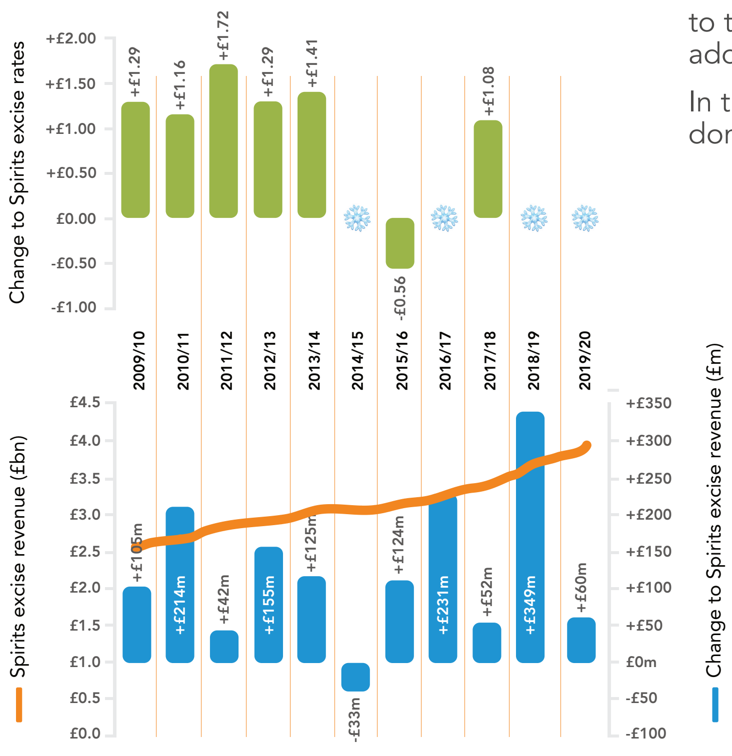
Scotch Whisky is a domestic success story. The industry contributes £5.5 billion to the UK economy, employs 11,000 people in Scotland and supports over 40,000 jobs across the UK. Our productivity stands at over £200k per employee, making Scotch Whisky more productive than the energy sector, life sciences or the creative industries.

Over more than 150 years of exporting, the industry has overcome many challenges. But the past eighteen months has been like no other period in the industry's history, and the industry has undoubtedly been damaged by a combination of US tariffs and Covid-19.

A cut in spirits duty is critical in helping the industry to recover and grow. It will enable the industry to be a partner in recovery. It will boost consumer confidence. It will support the hospitality industry - especially pubs and restaurants which rely on spirits to generate 15.7% of total revenue. And, importantly, it will raise more revenue for government to continue to support the economy through Covid-19.

The real-world HMRC data provides the evidence. Recent freezes and cuts to spirits duty have driven increased spirits revenue – HMRC receipts were up by 1.6% in 2019/20 building on a 10.2% increase in 2018/19. Following the 2% cut in 2015, receipts increased by 4.1%.

Spirits excise rates and annual revenue

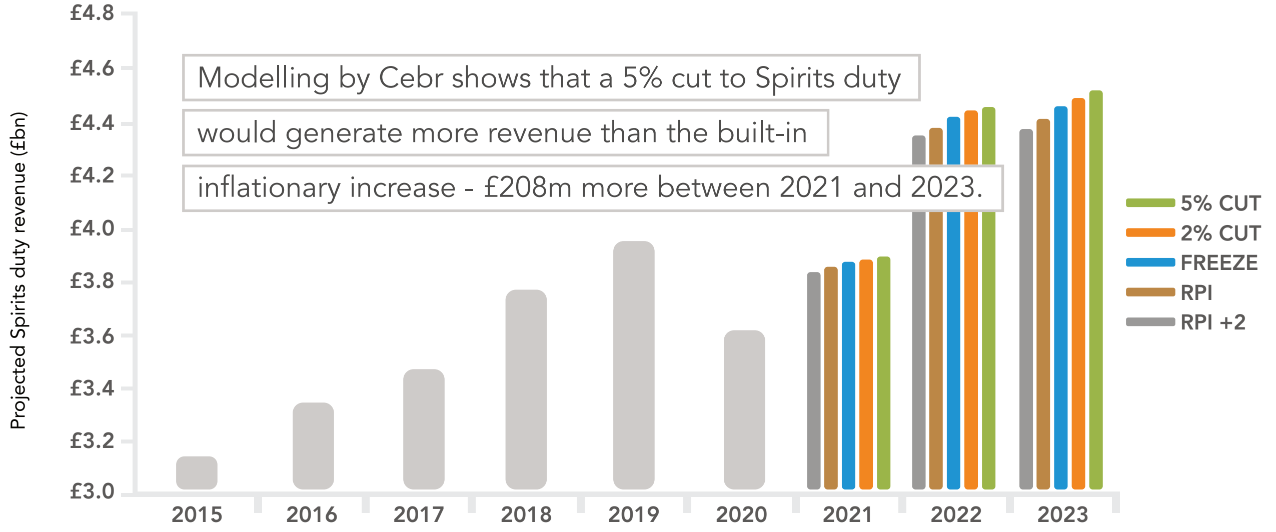


Source: HMRC/SWA analysis

Recent modelling, conducted by the Centre for Economic and Business Research (Cebr), shows that a 5% cut to spirits duty could increase duty receipts by £42m in year 2021, £70m in 2022 and £96m in 2023 compared to the built-in RPI increase. When duty and VAT are taken together, a 5% spirits duty cut will deliver £748m in additional revenue to government over the next three years.*

In the March budget, the Chancellor should cut spirits duty to grow public finances and support a key domestic industry.

* The analysis was carried out in late August and September 2020 and does not take account of recent Covid developments and related economic data. The highly uncertain economic environment therefore needs to be borne in mind when looking at these figures – which could be subject to change.



Source: Centre for Economic and Business Research

SUPPORT THE SUPPLY CHAIN

The Scotch Whisky industry supports over 8,500 supply chain companies across all four nations of the UK.

This represents 95% of the industry's total global supply chain - meaning that when the industry is backed in the budget, UK based companies benefit.

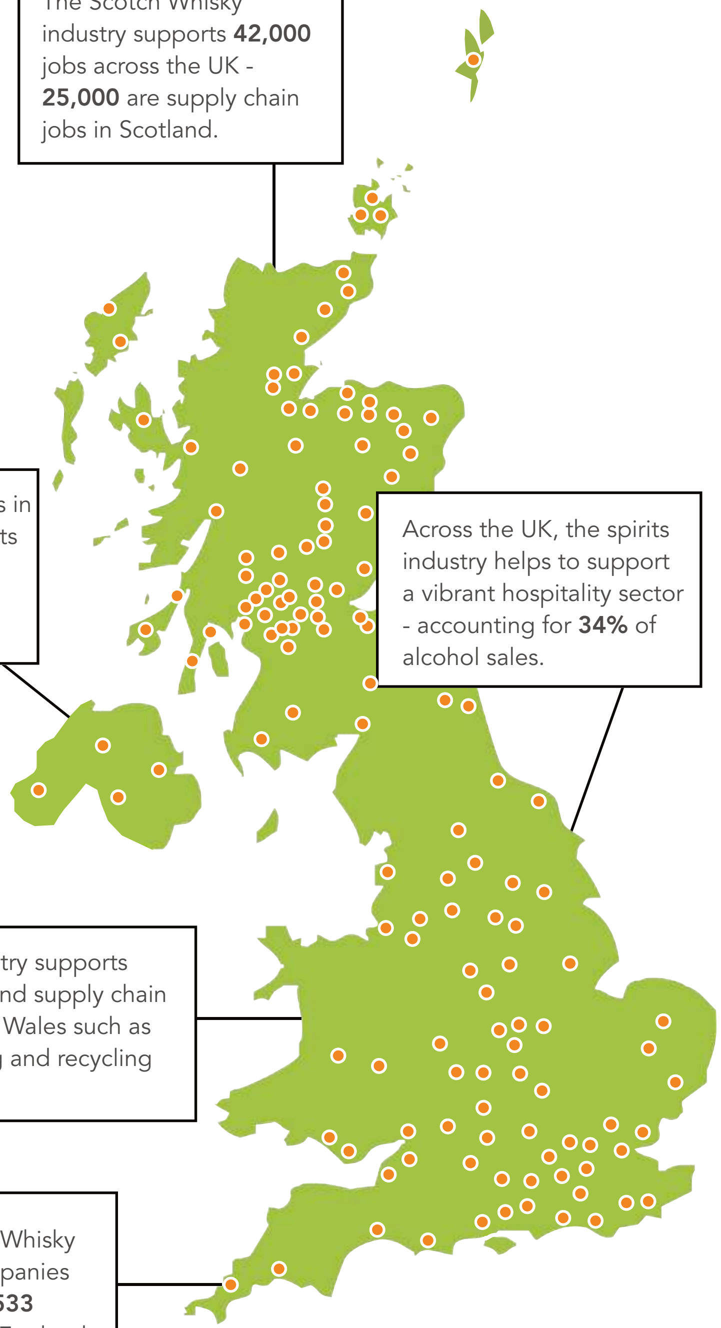
By supporting Scotch Whisky through a duty cut, the Chancellor can help to fill the order books of companies in every part of the UK - from marketing and logistics to raw materials and professional services.

Support in the Budget also gives our member companies confidence to invest across the UK. Past freezes and cuts in spirits duty have helped distilleries to invest over £1bn in distilleries, bottling halls and tourism facilities during that time.

Of course, the Scotch Whisky industry - and other spirits producers - form an important part of the hospitality supply chain. A cut in spirits duty would support the hospitality industry - especially pubs and restaurants - which rely on spirits to generate 16% of total revenue, and 34% if food sales are excluded.

The hospitality industry has been one of the worst impacted by Covid-19. The March budget is not the time to further increase the tax burden on hospitality businesses - but to extend support through a duty cut, and continued furlough, VAT relief and business rate holidays.

The Scotch Whisky industry supports **42,000** jobs across the UK - **25,000** are supply chain jobs in Scotland.



The industry's investments in renewable energy supports biomass technology and engineering services in Northern Ireland.

Across the UK, the spirits industry helps to support a vibrant hospitality sector - accounting for **34%** of alcohol sales.

The industry supports services and supply chain activity in Wales such as marketing and recycling services.

There are Scotch Whisky supply chain companies based in **338 of 533** constituencies in England.

PLAYING OUR PART

The Scotch Whisky industry is proud to have played a part in supporting frontline health services, emergency services, local communities and other industries through Covid-19 with the provision of hand sanitiser and ethanol.

Many of our member companies continue to manufacture hand sanitiser or provide high strength ethanol to other manufacturers. The SWA's **Hand Sanitiser Portal**, launched in March 2020, helped distillers to source necessary ingredients and organisations in need of sanitiser to find supplies when demand was at its highest.

The portal has now been live for over nine months, and the response from across the UK and overseas, particularly in the early stages of the UK outbreak of Covid-19, has been overwhelming.

Over 170 organisations have submitted their details and at the peak of demand, our figures show that pledges via the SWA Hand Sanitiser portal totalled more than 1.5m litres of ethanol a week, enough to produce over 12m 500ml bottles of hand sanitiser a month. This is in addition to the hand sanitiser that many distilleries have been producing to meet local needs in their communities.

In addition, as many tourism and hospitality businesses prepared to re-open, the industry shared its experience and expertise to help safely get the economy back up and running. The SWA set up a **Community Mentor Gateway** to connect businesses with members of the Scotch Whisky workforce to share advice and ideas - from developing risk assessments to sourcing protective equipment, safely managing spaces to ensure social distancing, to just being a friendly sounding board.

We were happy to be able to share the industry's experience at home, and in our overseas markets, to support businesses, communities and the economy during a time of crisis.

Thanking the industry, Secretary of State for the Environment, Food and Rural Affairs, George Eustice, said ***"When we put our minds to it, we really can get stuff done."***

It should be in that spirit that decisions are taken in the budget - industry and government working in partnership to support the economic recovery.

1.5m

At peak, 1.5m litres of high-strength ethanol
was pledged via the SWA's hand sanister portal -
enough to produce a bottle of hand sanitiser for every household in the UK.

Hand Sanitiser produced by Whyte & Mackay


Lindores Abbey Distillery

Hand Sanitiser being produced in a Bacardi laboratory

COCKTAIL CULTURE

The first lockdown period was predicted to cause a sharp rise in alcohol consumption and binge-drinking. However, Portman Group data shows the majority of UK drinkers (65%) actually drank the same, less or stopped drinking altogether during lockdown compared to same period in 2019.

Nielsen data also shows that between 16 March and 11 July 2020, the period covering the first lockdown, UK drinkers consumed 35% less than in the same period (1.3bn litres of alcohol in 2020 compared to 2bn in 2019.)

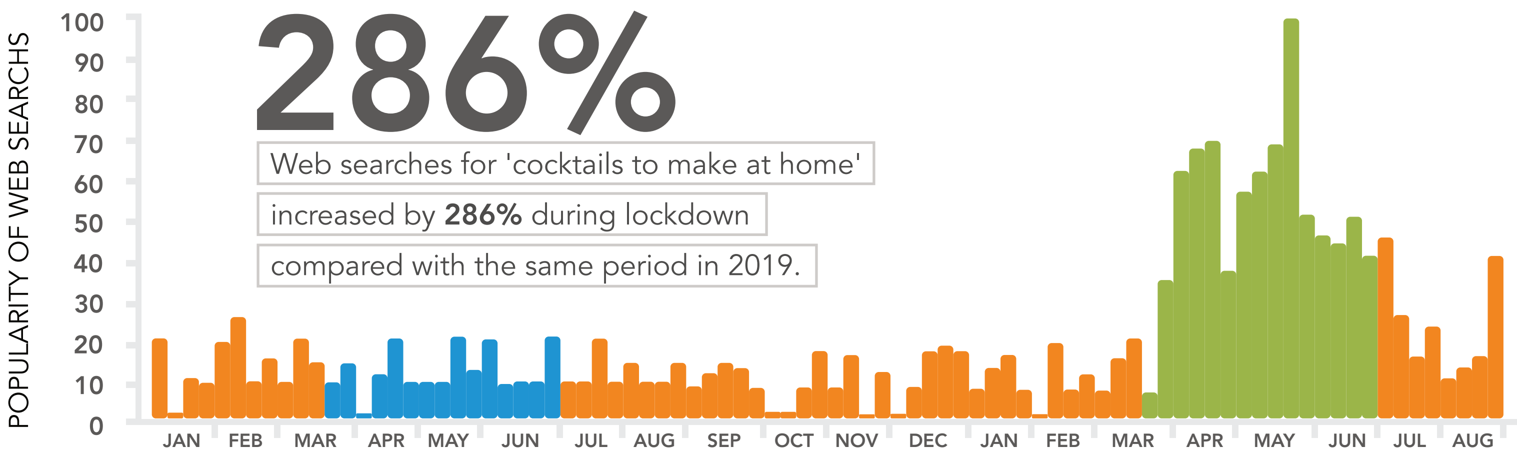
Consumers continue to drink less and drink better.

While alcohol revenue remains in flux due to the impacts of Covid-19, one trend that has emerged is continued premiumisation across the spirits industry. In the on-trade, spirit sales have increased as a proportion of hospitality industry revenue over the past five years. According to a recent report by Gerald Edelman, this has been caused by the increase in cocktail bars and premium decorative drinks.

Existing trends towards at-home cocktail making have been accelerated by consumers during Covid-19, with web searches for home cocktail kits up by 286% over the first lockdown period.

Online spirits sales increased by 23% in March compared with the previous year, accelerating the pre-Covid e-commerce trend in the UK with online alcohol sales growing four times faster than in physical shops. Kantar data shows that gin and Single Malt Scotch Whisky performed strongly during the lockdown period.

Premiumisation benefits HM Treasury - generating more in tax per unit of alcohol consumed. Ministers should resist any attempt to introduce additional taxes on e-commerce which would see this welcome trend stagnate.



Source: Google Trends

FAIRNESS FOR CONSUMERS

SCOTCH WHISKY TAX BURDEN	
Excise Duty	£8.05
VAT	£2.50
Total Tax (70%)	£10.55
Scotch Whisky (30%)	£4.46

Source: Tax burden based on average off-trade price of 70cl Blended Scotch Whisky at £15.01; Nielsen, August 2020

The Scotch Whisky industry is committed to helping consumers make responsible choices about alcohol consumption. We think that the tax system should do the same.

Differences in how excise tax is calculated for different categories causes large inconsistencies and is unfair for consumers. For example, on a per-unit of alcohol basis, tax on wine and wider decreases as the alcohol content increases. 11% ABV wine is taxed at 27p, while 15% wine is taxed at 20p. For cider, 4% ABV product is taxed at 10p per unit, while high-strength 7.5% ABV product is taxed less than 7p per unit.

The Chief Medical Officers' (CMO) guidelines on low-risk consumption say adults should drink no more than 14 units a week of alcohol. The guidelines do not discriminate between categories of alcohol, but the tax system does.

As a result, consumers who choose to drink 14 units of cider a week are taxed £1.13, those who choose to drink 14 units of wine are taxed £3.36, while those who choose to support Scotch Whisky are taxed £4.06.

Spirits, including domestic products such as Scotch Whisky, are taxed 256% higher per unit than cider and 16% higher than wine.

Cutting spirits duty in March 2021 will begin to reduce these competitive distortions and would be a step in the right direction, ahead of full reform of UK alcohol taxation committed to by the UK government.

We think a reformed tax system should be in place by autumn 2021 - and that the Chancellor should commit to a firm timetable for reform in the March budget.

A simplified and fairer system based on robust economic reasoning is expected to increase competitiveness and allow alcohol categories to compete over market share on a level playing field.

This would benefit consumers, boost employment in the domestic alcohol industry and remain an important driver of tax revenue.

> ***"We will... review alcohol duty to ensure our tax system is supporting Scottish whisky and gin producers and protecting 42,000 jobs supported by Scotch across the UK."***
>
> Queen's Speech; Dec 2019

Did you know?

There have only been four cuts to spirits duty, by three Chancellors, in the last 100 years! Will Rishi Sunak join the club?

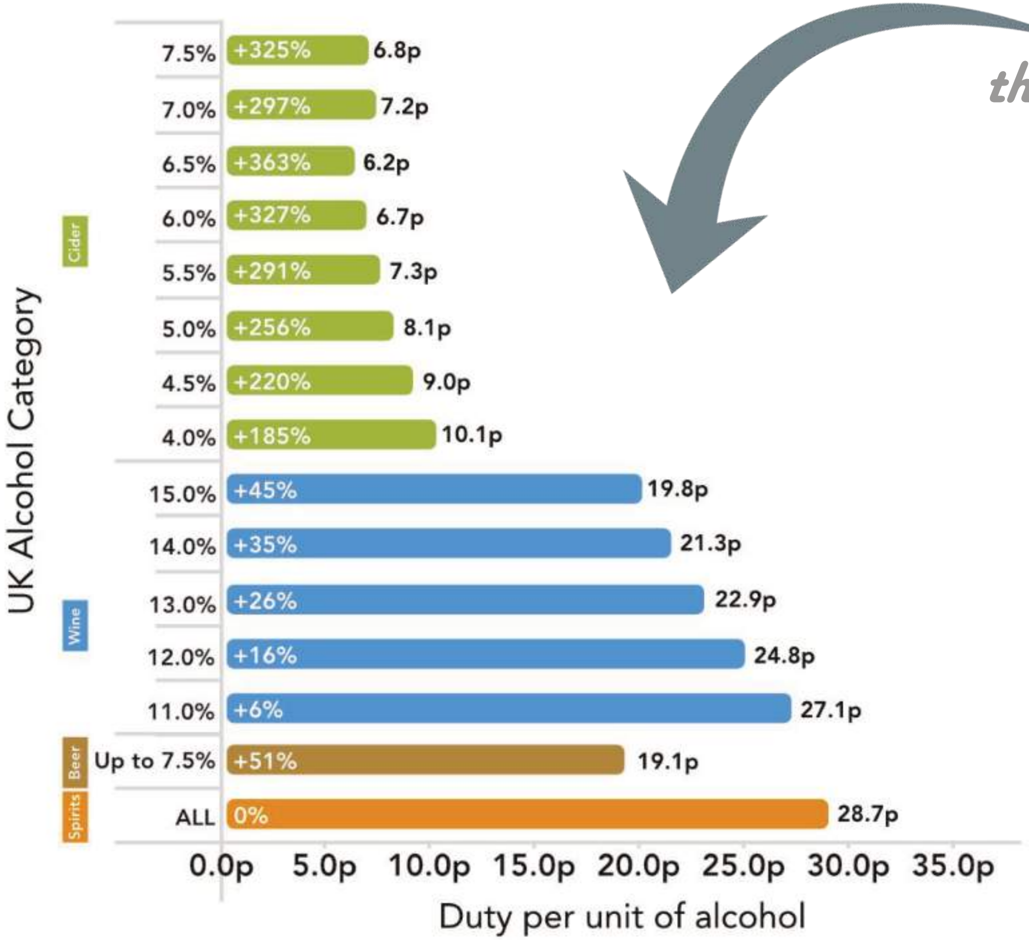
Anthony Barker
1973

Ken Clarke
1994

Ken Clarke (again)
1995

George Osborne
2015

Rishi Sunak
2021



"When compared on per unit basis the duty system as a whole is highly inconsistent."

HMT Alcohol Duty Review; Sept 2020

With the Alcohol Duty Review underway, the Chancellor should reject any action which further increases the competitive disadvantage faced by Scotch Whisky and other spirits in the UK.

HM Treasury, in the recently completed 'Call for Evidence', admits that the current system is "highly inconsistent" - that inconsistency should not be compounded in the March Budget.

The Chancellor should instead use the March budget to begin to address, in a phased approach, some of the inconsistencies and irregularities that have arisen in the alcohol tax system.

For example, per-unit of alcohol, tax on wine and cider decreases as the alcohol content increases. 11% ABV wine is taxed at 27p per unit, while 15% wine is taxed at 20p per unit. For cider, 4% ABV product is taxed at 10p per unit, while high-strength 7.5% ABV product is taxed less than 7p per unit.

While these structural anomalies should be fixed as part of the duty review, the March budget is an opportunity to bring about greater fairness for Scotch Whisky through a duty cut.

LEVELLING UP IN SCOTLAND

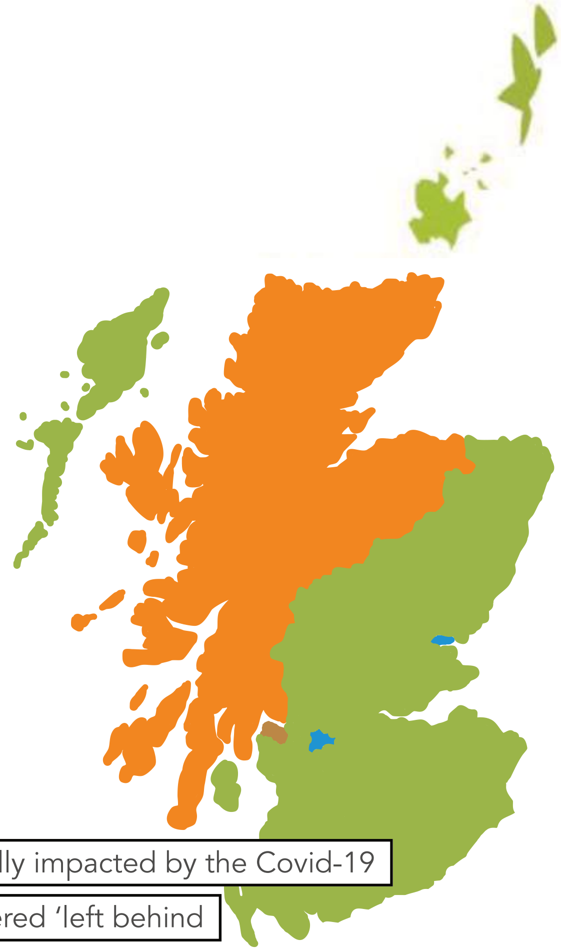
It's the people and places of Scotland that make Scotch Whisky what it is.

The UK government's 'levelling up' agenda is about rebalancing the economy, and supporting those areas that have been overlooked for government support. The Institute for Fiscal Studies (IFS) has found that the UK "is one of the most geographically unequal countries in the developed world; compared with 26 other developed countries, it ranks near the top of the league table on most measures of regional economic inequality."

This includes areas of Scotland. The IFS also concluded that Scotland's rural areas have relatively low employment rates compared to the rest of the UK, and pay is notably low.

And it would be worse if it wasn't for the Scotch Whisky industry, which directly employs 11,000 people in Scotland, many in rural or fragile economic areas.

Support for the Scotch Whisky industry is support for the levelling up agenda - ensuring that those areas of Scotland, particularly rural communities and the people that live there, are supported through employment, investment and opportunities.



Areas economically impacted by the Covid-19 crisis and considered 'left behind

Source: IFS Green Budget, Oct 2020

Top quintile for:

- **Covid-19 and 'left behind'**
- **'left behind' only**
- **Covid-19 only**
- **Neither measure**

Did you know?

70% of UK gin is produced in Scotland, much of it by Scotch Whisky producers.

Chancellor Rishi Sunak visited Copper River gin distillery in Kent in May.

Photo Credit: HM Treasury/Simon Walker

"The government will set out further details on how to support levelling up across the UK in the New Year."

HMT Spending Review Nov 2020

COMPETING ON THE WORLD STAGE

Scotch Whisky is the UK's largest food and drink export, accounting for 75% of Scottish food and drink exports, 21% of all UK food and drink exports, and 1.4% of all UK goods exports.

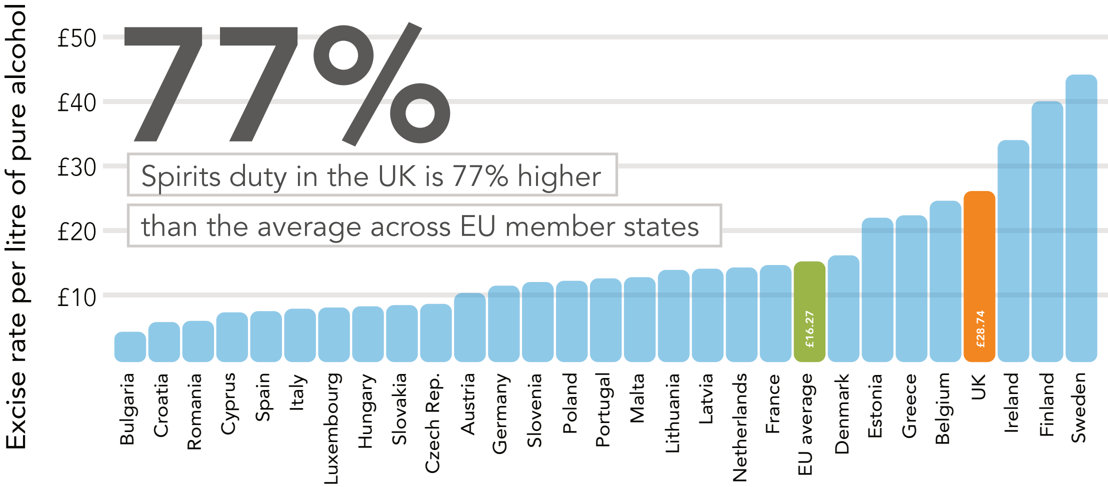
£1.1bn

Global exports of Scotch Whisky have fallen by 26% in the last year - a drop of £1.1bn to end of October 2020.

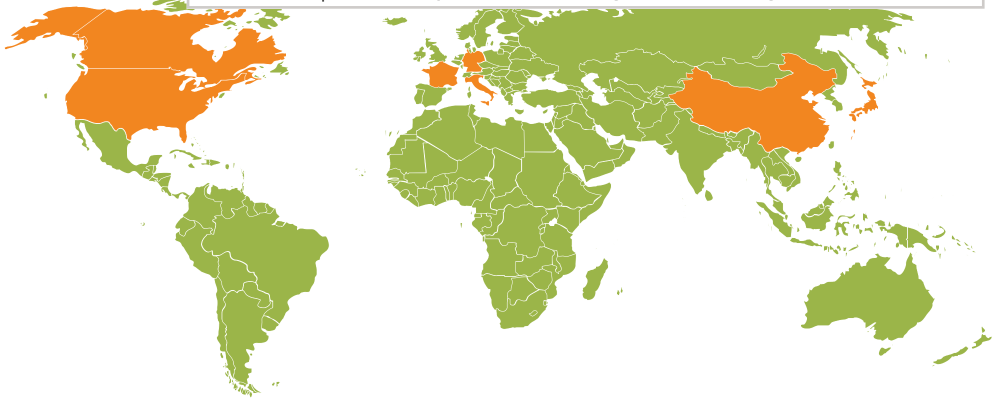
Across the global markets, the industry faces varying levels of spirits duty - but far from supporting a vital domestic industry, UK spirits duty on Scotch Whisky is one of the highest in the world. UK spirits duty is almost double the rate in France, triple the rate in South Africa, and four-times more than in the United States. Exchequer Secretary Kemi Badenoch MP has said: "now that the UK has left the EU and is free to set its own law in this area, I believe that we can shape our duty regime in the best way to suit our national priorities." We agree, but the starting point remains a UK spirits duty rate that is 77% higher than the EU average.

Supportive tax treatment for Scotch Whisky, starting with a duty cut in March 2021, will be critical if the industry is to bounce back as quickly as possible from the expected 25% drop in global exports caused by tariffs and Covid-19. This will help ensure too that we do not face an increased risk of further tax increases in key export markets. For example, after HMT increased duty on spirits by 3.9% in the 2017 Spring Budget. Two weeks later, Canada increased duty on spirits by 2%, followed by the Kenyan government increasing duty on spirits by 14.3% on 30 March. In both cases, when Scotch Whisky producers challenged these tax increases, they were told to address the tax burden in our home market before addressing tax rates in export markets.

Budget decisions made by the UK government send a strong signal to governments overseas - and the Chancellor should cut spirits duty to make the UK government's support for Scotch Whisky clear to global markets.



Across major global economies, the UK has one of the highest rates of spirits duty - and the highest among G8 countries.



PAYING THE PRICE OF TARIFFS

"Scotch Whisky is a crucial industry and our largest food and drink export. My colleagues have highlighted to me the impact that the recent US tariffs are having."

Chancellor Rishi Sunak; March 2020

Since Chancellor Rishi Sunak said this in March last year, the industry has continued to lose hundreds of millions of pounds in exports and market share due to a trade dispute that has nothing to do with the Scotch Whisky industry.

The ongoing impact of the 25% tariff on Single Malt Scotch Whisky exports to the United States has been devastating for the industry. The US has been Scotch Whisky's largest and most valuable export market for decades, and – until the imposition of tariffs – a growth market for Single Malt.

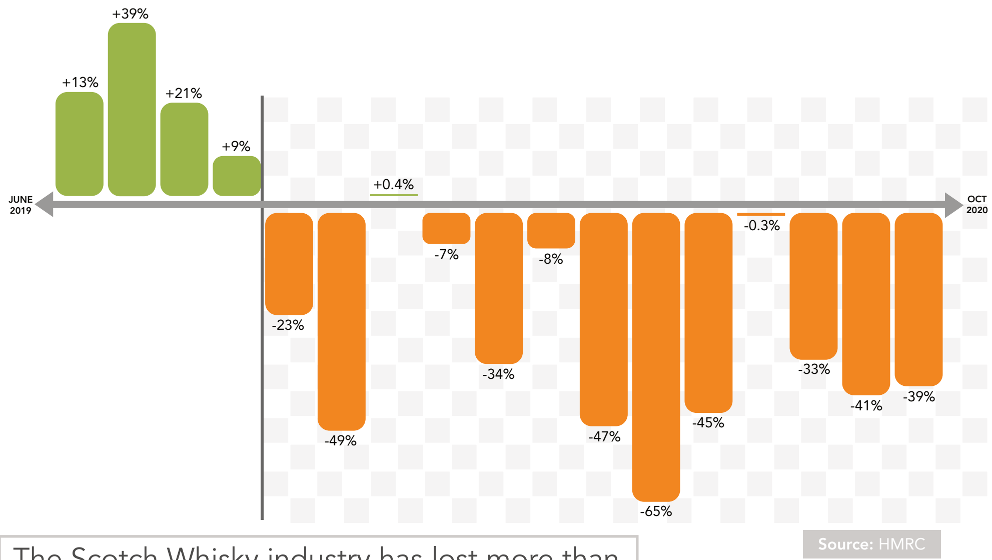
In the 15 months since the tariff came into effect, exports of Scotch Whisky to the US have fallen by 32%, amounting to over £450 million in lost exports.

These losses have been compounded by the impact of Covid-19 in the US, with the closure of bars and restaurants also depressing exports.

This is all causing distillers real concern, with the impacts falling disproportionately on smaller producers, many of whom are now finding it impossible to export to the US at all, as importers are concerned about selling their Single Malts at raised prices in a severely disrupted market.

This is creating real pressure on businesses and jobs and risk long term damage to the industry

Exports of Scotch Whisky to the United States



The Scotch Whisky industry has lost more than £450m in exports to the United States - the industry is paying the price for a trade war not of our making.

We now urgently need the support of HM Treasury.

The Chancellor must now go further than the duty freeze last March, which recognised the impact of tariffs on the industry at that time. The ongoing damage caused by US tariffs means that a duty cut is now imperative to support the industry.

INVEST IN A GREEN RECOVERY

The £10 million fund, announced in the March 2020 Budget, to help Scotch Whisky distilleries go green by switching to low carbon fuels such as hydrogen was welcome recognition of the significant steps that must be taken to achieve our net-zero ambitions.

This funding will enable distilleries to test innovative and emerging low carbon technologies which will be needed for us to achieve our net zero ambitions.

But we must go further - and by building on the Green Distilling Fund in the March Budget, the UK government can underpin the progress that has already been made by the industry in ensuring a more sustainable future for Scotch Whisky.

The Chancellor should take the opportunity following the Covid-19 pandemic to rebalance the economy in favour of industries that take sustainability seriously.

Over the last decade, the industry has been an environmental leader - reducing greenhouse gas emissions by 34%, increasing renewable energy use from 3% to 28% and improving energy efficiency by almost 10%. At the same time, the industry has increased production and exports. This is the kind of productivity, with green ambitions at its heart, that should be incentivised by the UK government.

A cut in spirits duty will enable the industry to invest more in further reducing Scotch Whisky's environmental footprint, while continuing to deliver significant revenue, investment and employment in the UK economy.

LIFT THE NATION'S SPIRITS - CUT DUTY

We are in one of the most challenging periods any of us can remember.

The global pandemic has put strain on the UK economy and has strained people across the country as continued restrictions keep us from friends and family, and enjoying the simple things we have taken for granted, like a visit to the local pub.

At the start of 2021, the Scotch Whisky industry, the hospitality sector and the country as a whole needs a boost. And the Chancellor can deliver one in the budget on 3 March by cutting spirits duty.

A spirits duty cut would:

Deliver more revenue for government to help the UK's economic recovery

Modelling shows that a spirits duty cut would deliver more revenue for government than a freeze or inflationary increase - up to £750m more with a 5% cut.

Keep the UK government's promise to do all it can to support the Scotch Whisky industry suffering from US tariffs

The Scotch Whisky industry has lost more than £420m in exports to the United States after 15 months of tariffs. The UK government must provide support for the industry while it continues to pay the price for trade disputes not of our making.

Support communities across Scotland as part of the 'levelling up' agenda

The Scotch Whisky industry provides vital employment and investment for communities across Scotland - particularity in rural and island communities. Supporting the industry to sustain jobs and investment will be key to the post-Covid economic recovery.

CHANCELLOR, LIFT THE NATION'S SPIRITS - CUT DUTY

The Prime Minister has committed to supporting the Scotch Whisky industry.

Photo Credit: PA/Stefan Rousseau

At a glance: Scotch Whisky industry economic contribution to the UK

Over two-thirds of UK spirits GVA is generated by Scotch Whisky

The UK's balance of trade deficit would be 3.3% wider without Scotch Whisky

Scotch Whisky accounts for 21% of all UK food & drink exports

The industry employs over 42,000 people across the UK