

Alcohol Industry Concerns & Opportunities Related to the BC Liquor Distribution Branch

Prepared By:



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Our Mandate

Cascadia was retained by a number of alcohol industry participants in BC due to immediate and serious concern over lost business opportunities. The mandate was to investigate common industry views related to the BC Liquor Distribution Branch.

Project Goals



Explore consensus issues among alcohol industry associations



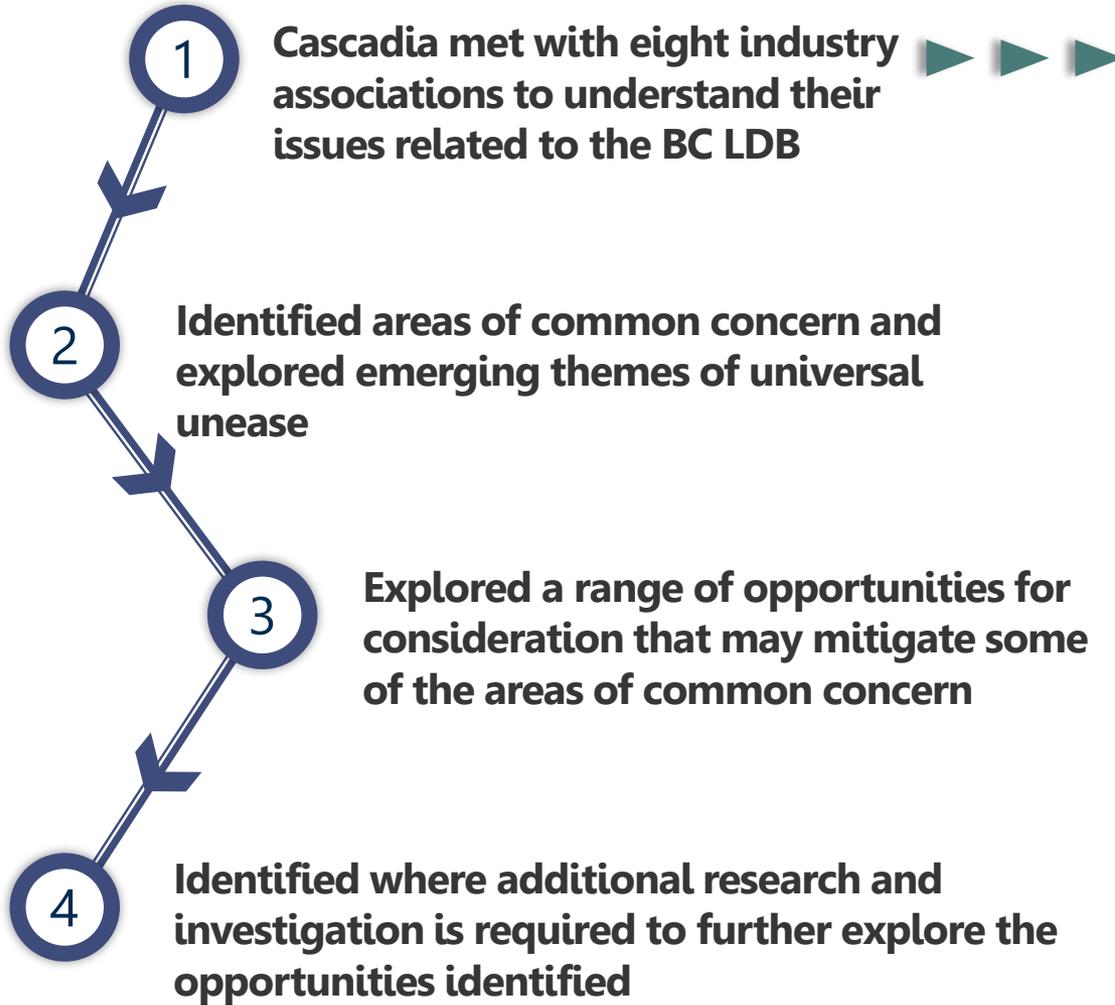
Identify the nature and breadth of issues



Categorize the Nature of Impacts by stakeholders

Some important industry association issues are not collectively shared by the broad group of industry associations that participated in this exercise. Cascadia's intent is not to minimize these issues, which we have identified in this document, rather to focus on collective industry challenges. Specific items are noted at the end of this material, and we expect the respective industry associations to bring forward their specific points individually.

Our Approach



Industry Association Consultations



Issue Summary

There were five key issues that were universally identified among the industry associations that were consulted:



1. Corporate Structure of the LDB

The nature of the warehousing and distribution monopoly combined with a large competitive retailer within one entity was identified as a key concern.



2. Warehousing and Distribution Challenges

Sub-optimal inventory management has led to repeated stock-outs and additional handling and inventory expense borne by the consumers and industry participants.



3. Retail Pricing Concerns

Retail prices are not transparent and changes are introduced without proper notice or consultation, impacting producers as well as retailers who require greater certainty.



4. Data Availability and Sharing

BC is seen as one of the jurisdictions with the least availability and transparency of data necessary to manage and monitor sales, trends, and marketing campaigns.



5. Cannabis Impact on Alcohol Sales

Cannabis has been known to be a substitute for alcohol. To this end, Cannabis tax revenue forecasts need to factor in lower alcohol tax revenue.

Corporate Structure of the LDB



Context and Industry Impact

The existing LDB structure, as both a state owned monopoly on alcohol warehousing and distribution as well as a competitive retailer is of significant industry concern. There is a recognition that the LDB has taken some steps through reporting structures to remedy this, but it is also a widely held view that additional steps should be taken to ensure that the mandate of the LDB is clear and transparent.

It is critical that the LDB mandate incorporates both its role as an important revenue source for the Province, but also as the steward of multiple high value agriculture, hospitality, and tourism industry sectors. It is our belief that the next three issues: Warehousing and Distribution Challenges, Retail Pricing Concerns and Data Availability and access are direct result of the existing LDB structure.

Options for Consideration

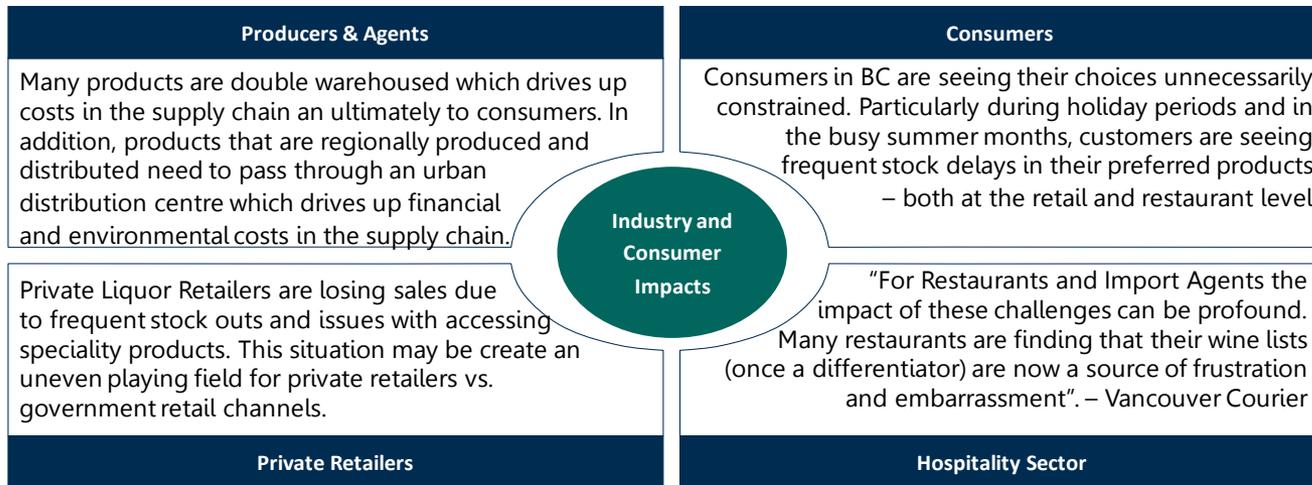
- Introduce a Board Of Governors for the LDB that would allow for industry, community, and consumer representation. This Board could act in Advisory capacity to assist LDB in fulfilling a broader public mandate.
- Develop a balanced set of transparent metrics for the LDB that represent the complex set of diverse social and regional economic interests that a modern liquor distribution and retailing system requires.

Warehousing and Distribution Challenges



Context and Industry Impact

While there was recognition that LDB has experienced challenges related to a new system implementation, they believe that current processes and inventory management practices fail to meet modern standards. Specifically, those interviewed have significant challenges with frequent stock outs, difficulties accessing specialty products and double handling of goods, which are warehoused in the private system and then handled by LDB prior to end distribution.



We recommend the LDB consider opportunities to leverage private distribution handlers and explore whether the all or nothing opt-in model remains relevant.

Options for Consideration

- Explore the use of bonded logistics firms already operating in the marketplace to augment LDB capacity during peak demand periods or for specialty goods This would allow for more consistent service times and equal treatment between the multiple groups of retailers.
- Apply common sense exceptions to distribution model rules when it benefits other provincial objectives and consumers

Retail Pricing Concerns



Context and Industry Impact

The LDB Retail pricing approach is causing significant challenges for those we interviewed. The primary challenges relate to three issues.

- 1) Retail pricing variability for the hospitality sector.** The LDB adjusts prices as a competitive retailer, but the hospitality sector needs to plan menus in advance and seeks to service a range of price points with their offerings.
- 2) Adjusting the retail mark-up of products on-shelf.** The current practice of increasing retail mark-up for better moving products is damaging to producers and agents. Producers and agents set price points based on planned inventories, marketing plans, and matched products. Unexpected changes in retail pricing are creating an imbalanced competitive environment and contributing to inventory challenges for producers.
- 3) Bridge Buying.** Industry participants we interviewed indicated many examples of the LDB taking advantage of limited time offers to purchase more inventory at the LTO price than they anticipated selling during the LTO period. This practice should be stopped as it is unfair for LDB to use its position as a monopoly on inventory management to drive additional retail profits. In the consumer goods industry this additional mark-up is typically returned to the product owner or reinvested in other retail promotional opportunities.

Options for Consideration

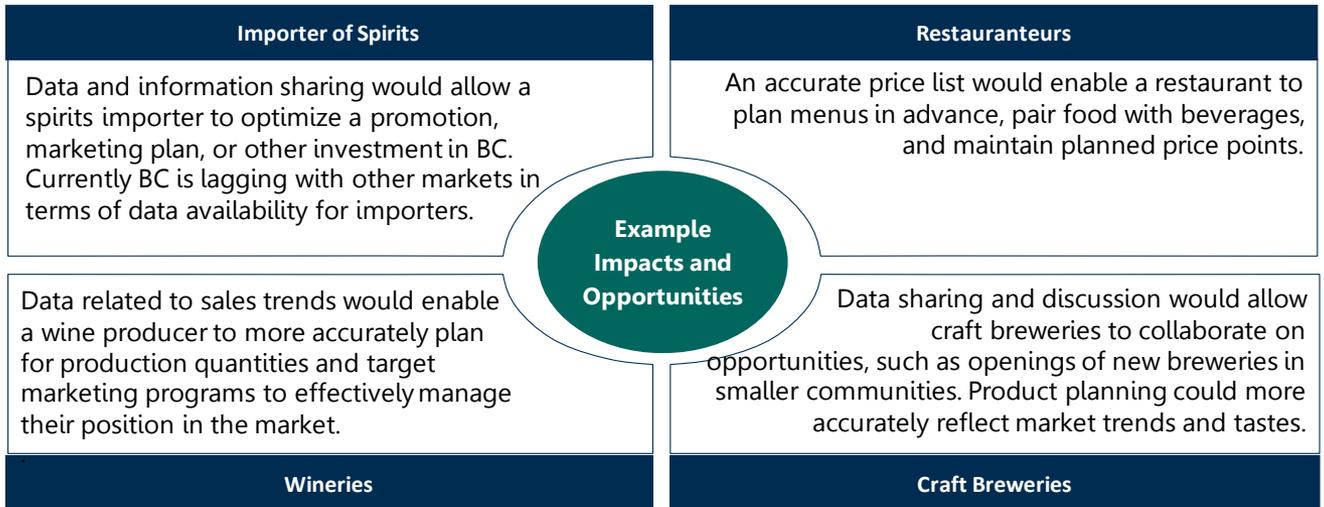
- Introduce a fixed retail price markup for the hospitality sector that is below retail store markups to provide certainty and consistency for the sector
- A range of options that provide greater price certainty which spans from fixed retail mark-ups to consultation with industry participants prior to introducing retail pricing changes
- Ensure that the LDB passes along to BC consumers the full value of all inventory purchased with a supplier funded wholesale price reduction and not assume investments intended for consumers

Data Availability and Sharing



Context and Industry Impact

One of the impacts of the current LDB corporate structure is that some industry stakeholders, namely private retail, is competitive with the LDB retail channel. This has led to less industry information sharing which has a negative overall impact on the industry as a whole. Those we interviewed have limited access to pricing and volume figures that would allow them to work with the LDB to effectively market and plan products development.



We recommend the LDB explore opportunities to increase data and trend information sharing to allow partners to better manage their businesses.

Options for Consideration

- Explore best practices in other jurisdictions and make data sharing and industry collaboration a priority, particularly for the warehousing and distribution channel

Cannabis Impact on Alcohol



Context and Industry Impact

In other jurisdictions where recreational marijuana has been legalized, it has been demonstrated that alcohol sales were reduced as cannabis sales increased. In other words, cannabis has been shown to be a substitute good for alcohol.

The industry associations are concerned that Provincial cannabis tax forecasts will be prepared in isolation of alcohol mark-up and tax forecasts. Preparing these forecasts in isolation would fail to capture the substitution effect of cannabis on alcohol and may lead to lower than expected alcohol tax revenues. This would be a negative outcome for both the Provincial Government and the alcohol and beverage industry in the province.

A second concern is manner in which recreational marijuana will be retailed within the LDB if this is the distribution channel adopted by the provincial government.

Options for Consideration

The BC government needs to better understand the cannibalization effect that recreational marijuana will have on provincial alcohol sales. The LDB should conduct a study using existing markets with recreational cannabis as a guide to understand the likely decrease (short and long term) in alcohol sales and make sure the decrease in expected revenue is anticipated by the Finance Ministry.

Individual Association Issues

The following issues were unique to each industry association and while important, each association will provide additional details on these issues separately from this collective exercise.



BC Craft Distillers Guild

- Higher thresholds (currently 50,000L) on mark-up free 100% made in BC craft farm-to-flask distillery products
- Mark-up rebate should apply to 100% BC farm-to-flask products
- Economic study to determine the regional economic benefits associated with farm-to-flask production
- To drive consistency in policy development and application, develop industry leadership to bring a single view of craft (Beer, Wine, Spirits) to work with government on mutually beneficial growth



BC Alliance of Beverage Licensees

- Permit 'License Sales' facilitating purchases by restaurants and other liquor primary establishments directly from private liquor stores that can service in the quantities and timelines needed for the industry



Import Vintners & Spirits Association

- Eliminate retail mark-ups for product sampling aimed at product education



Spirits Canada

- All concerns related to the BC LDB are reflected in the consensus concerns detailed earlier in this report

Individual Association Issues

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BC Craft Brewers Guild

- The quantities from contract manufacturers that brew on behalf of other craft breweries should be assigned to the purchasers annual volume for markup threshold purposes
- Investigate the Made in BC Craft policy to reflect the reality that 100% of beer inputs can not be sourced within BC



BC Wine Institute

- Index the minimum price set for alcohol purchases to inflation
- Pursue a 'buy local' mandate for the LDB retail division
- Maintain existing programs that support the BC Wine industry (VQA through grocery channel)



BC Restaurant & Food Service Association

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Restaurants Canada



- Lack of a wholesale pricing model for restaurants hurts business
- Restaurants currently pay the LDB retail price or higher (LTOs not passed through) for beer, wine, and spirits. In a low margin business, this makes it challenging to stay afloat and leads to negative customer experiences
- Combined with difficulties in accessing inventory and unexpected variability in pricing, lack of wholesale pricing is undoing much of the positive progress from the liquor reform modernization in 2015

About Cascadia Partners

Cascadia Strategy Consulting Partners provide strategy, economic, and financial analysis to a broad-cross section of government and industry clients.

Cascadia helps clients advance major initiatives and solve complex business challenges. Our team has a proven track record analyzing and solving critical challenges in highly complex industries. Advancing complex initiatives requires a clear understanding of economic impact. Cascadia provides leading expertise in economic impact assessment, revenue/cost forecasting, and sensitivity analysis.

Meet Our Team



Paul Hiom
Partner

Paul has more than 20 years of consulting experience in strategic analysis, corporate planning, capital planning and operations analysis. He is a former Lead Partner for Western Canada for SECOR Consulting, and the former Lead Partner for Advisory Services in BC for KPMG Consulting.

Paul has worked extensively with clients in a broad cross-section of industries, with a focus on complex logistics challenges in health care, transportation, energy and telecommunications.



Jonathan Snoek
Partner

Jonathan's 15 years of management consulting experience has included: strategic planning, financial modeling and analysis, business transformation and technology replacement (planning, project management, and execution), operations analysis, and market research. Jonathan was a Senior Manager in KPMG's strategy consulting group.

Jonathan has worked with more than a dozen industry associations helping advance their interests with analytics, economics, and market research.



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