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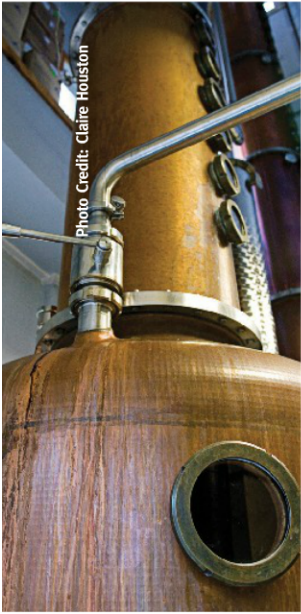
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Small craft spirits producers take a page right out of brewing history and distill a hand-crafted, artistic revolution all their own.



The Spirit of Invention

Craft distillers bring passion and innovation to their burgeoning segment. **By Jeff Cioletti**

You all know the familiar refrain. For decades beer has been surrendering considerable market share to spirits (as well as wine). It's seemed that the one upbeat narrative the beer industry could hang its hat on has been the explosive resurgence of craft brewing during the past decade. But it seems these days the spirits category has been attempting to steal a little of that thunder as well with the emergence of its own artisanal arm.

"Macro consumer trends are pointing to the search for new experiences with the products that are consumed," says Brian Sudano, managing partner of Beverage Marketing Corporation and BMC Strategic Associates. "That's what's supporting craft beer. And at the same point you're starting to see the movement toward craft distilled spirits."

In many ways, the similarities between what's going on now with artisanal distilling and craft brewing's origin story are striking. Think back to the late '80s and early '90s when craft beer had its initial boom. "[Craft beer] was really little and then it started to gain momentum," recalls Sudano. "It took a while before it hit about two and a half share, flattened out for 10 years and then grew again. We're starting to see similarities with craft spirits that we saw with craft beer in the '80s and '90s."

The Latest Tally

The exact number of craft distilleries in the country varies, depending on whom you're asking. According to Bill Owens, presi-

dent of the American Distilling Institute (ADI), which represents craft distillers, there are 400 craft distilleries in the U.S. (and a good 20 or so more in Canada) with another 50 or so under construction. (That's still relatively small in comparison to the number of craft breweries in the U.S.—about 2,100 at last count, with another 1,200-plus in planning.)

However, Dave Pickerell, the former master distiller at Maker's Mark, who now runs Oak View Consulting and has had a hand in the launch of some 23 operating craft distilleries with another six or seven in the works, says that 400 figure represents the number of permits that have been issued. The number of distilleries producing at this point in time is probably 100 fewer than that. "Some of those [400] have permits but no operations right now," Pickerell explains "Some of them are what we call merchant bottlers—they go and get the spirits and they bottle it, but someone else is distilling it."

The merchant bottler concept is not unlike contract brewing in the beer realm. "There are a lot of people whose model is to

CRAFT CLOSE-UP: Hillrock Distillery Farm to Bottle



In few companies is distilled spirits' agricultural heritage more apparent than at Hillrock. Founder and owner Jeff Baker grew up working on farms and ultimately established his own in Upstate New York.

"There were a number of things that sort of directed me toward what I'm doing," he recalls.

For one, he discovered that an old, recently restored house on one of his properties belonged to a Revolutionary War captain who was also a highly

successful grain merchant.

"There was a pretty good chance that someone was making whiskey out of all that grain," he says. "And I thought about what kind of value-add product we could make and better than anyone else."

During the course of his research into the craft distilling movement, one name kept popping up: Dave Pickerell, former master distiller at Maker's Mark, who now runs Oak View Consulting and has had a hand in the launch of nearly 30 micro-distilleries. Baker reached out to Pickerell and now Hillrock, whose products are just hitting the market this year, is among those. Pickerell is billed as the master distiller of Hillrock, whose management team also includes head of operations and distiller Timothy Welly.

"I realized no one was really coming close to doing a true field-to-glass operation like a high-end winery in Napa Valley, where they're effectively focused on the terroir of the location," Baker continues.

In addition to a distillery in the center of the farm in Ancram, N.Y., Hillrock also has its own malt house.

Hillrock currently offers rye and bourbon whiskeys, the latter of which employs the solera method. "It's traditionally used for aging fine sheries and some Scotches," he explains. "It's effectively a giant pyramid of barrels where you put younger whiskey in the upper barrels and you periodically take whiskey out of some of the lower barrels—effectively each barrel cascades down to the other barrels. You're never emptying any barrel; it allows the younger whiskey to merge with the much older, more mature whiskey, giving you tremendous complexity and some level of consistency." —J.C.

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"Certainly craft distilling is about mindset and outlook. But I don't know how you quantify entrepreneurial spirit to separate a big boy from a little guy." —DAVE PICKERELL, OAKVIEW CONSULTING

start out by bottling up what I refer to as 'found whiskey' and create a brand," Pickerell says. "And the goal is to use the profits that that generates to start funding the building of the distillery. So, discount 25, 30 who have permits but aren't really doing anything yet, discount another 50 or 60 for people that are bottling but not distilling and the real number is closer to 300 where there's really distilling going on."

That being said, craft distilling, Pickerell observes, is "absolutely on fire," with a new craft distillery opening up about once every other week.

A Question of Identity

As it has been with its brewing counterpart, craft distilling has wrestled somewhat with identity issues. The breweries worthy of the craft designation, according to the Brewers Association (BA), are independent (less than 25 percent owned or controlled by an alcohol beverage company that's not itself a craft brewer), use traditional methods—with an all-malt flagship brand or at least half of its volume from brews that are all-malt or use adjuncts "to enhance rather than lighten flavor"—and are small. The definition of "small" has been tweaked recently. There used to be a 2 million barrel ceiling, but the BA raised it to 6 million, largely because Boston Beer Co. had outgrown that 2 million barrel threshold.

On the distilling side of the artisanal world, the criteria are a little more open to debate. ADI's definition caps production at 65,000 proof gallons or about 34,000 cases a year. But even Owens concedes that that threshold could change. "Now we've got two or three people bumping up against that, so I'm sure we're going to raise it to 100,000 cases," Owens reveals. "You've got to remember 100,000 cases is an experimental batch done by one of the bigger distilleries. They'll roll out 100,000 cases of vodka just to test the market. For a [small] distiller to do 100,000 cases, you'd be quite wealthy."

To complicate things further, each state has its own idea of what constitutes a craft or micro distiller. "Some [states] say it's 50,000, some say it's 65,000, some say it's 100,000 and some of them have ignor-

mous limits,” says Pickerell. “When you actually go state by state, it’s about what the state is willing to give a license for. At the federal, it doesn’t matter, there’s no such thing as a craft license at the federal level.”

There are parameters other than volume, of course, but those are much harder to gauge in concrete terms. “Certainly it’s [about] mindset and outlook,” offers Pickerell. “But I don’t know how you quantify entrepreneurial spirit to separate a big boy from a little guy.”

Political Economy

There are a couple of factors—in both the public and private sectors—that have been helping craft distillers grow and likely continue to do so for the foreseeable future. On the public front, it’s the states themselves, as elected officials begin to recognize the economic advantages craft spirits producers create in their states.

“The more progressive states are beginning to realize there’s tax revenue, there’s tourism revenue, there’s jobs,” notes Pickerell.

He points to Oregon as a prime example of a state whose laws are friendly to artisanal distilling (not to mention craft beer, as Symphony-IRI has reported that craft represents close to 40 percent of overall beer revenue in the state).

“If you draw a circle 30 minutes from the center of town in Portland, there are 24 distilleries,” he points out.

Craft activity also is ramping up in the Northeast/Mid-Atlantic region. “It’s just getting started, but New York is exploding because New York has figured it out,” Pickerell observes. “There are distilleries all up and down the Hudson Valley now and as states figure it out, the industries begin to explode.”

There’s been a significant change in climate on the private front, as well, as spirits distributors increasingly embrace the artisanal upstarts—a shift similar to what happened with craft beer. The contrast between the distributor-distiller dynamic of today versus in 2005 when Philadelphia Distilling was just getting started couldn’t be any starker, says the distillery’s co-founder Andrew Auwerda. “When we first started pitching distributors, they didn’t really know what craft distilling was; they didn’t think of it as a separate thing,” recalls Auwerda. “People would roll their eyes when I said micro-distilling or craft distilling. I’d make an

CRAFT CLOSE-UP: Dulce Vida Spirits The Tex-Mex Connection

Richard Sorenson, founder and CEO of Austin, Texas-based Dulce Vida Spirits, entered the tequila world via another beverage route, albeit an unlikely one:

“We actually started in organic soft drinks in 2004,” he reveals.

The beverages the company was producing at the time were sweetened with blue agave nectar, the sourcing of which enabled Sorenson to get to know not just the organic agave farming co-ops, but tequila makers who were distilling with those farmers’ output.

The company divested itself of the soft drink business in 2007 and launched the tequila operation in 2008, completing its first small batch production run of the 100-proof, USDA-certified organic tequila in the summer of 2009.

“We sold our very first bottle in Austin in Sept. 2009 and it’s been kind of off to the races ever since,” he recalls.

Of course, in order for a product to be labeled tequila, it must be produced in Mexico.

“As Champagne is to France, tequila is to Mexico,” Sorenson points out. “There’s a geography border and a formulation border tequila, governed by the tequila regulatory council. If you violate the four walls of the sandbox, be it geography or formulation, you cannot be labeled as a tequila. Otherwise, you’re labeled as an agave spirit or mezcals.”

So how does a company based in the Lone Star State play in the sandbox? Through what’s called the maquila approach to production. The company’s Mexico-based master distiller and co-founder Carlos Jurado produces the organic tequilas in an existing facility about 90 minutes outside of Guadalajara, Mexico that Dulce Vida pays to use.

“[The concept] dates back 150 years to grain production, where people shared the facilities and paid for the use of the facility with a portion of the grain,” Sorenson explains.

The company contracts with a co-op of agave farmers—responsible for about 70 percent of Mexico’s agave exports—uses its own proprietary yeast and nutrients and performs the complete production run. It’s similar to gypsy brewing on the craft beer side, except the distiller is always using the same facility instead of moving around.

“We’ve got our own barrels that we brought down from Kentucky and we’ve got our own liquid aging,” he says. “We don’t buy somebody’s liquid. From a regulatory standpoint, it’s referred to as ‘alternate proprietorship.’”

Dulce Vida is the only company using space at that particular facility in such a way—beyond the facility’s owners—because of the master distiller’s relationship with the site’s owners.

In addition to meeting the stringent criteria for the tequila to be certified organic, the Mexican production facility itself is known for its sustainability efforts. “The heads and tails of the distillate are used along with the fiber from the agave; the liquid is pH balanced and then placed on the fiber and then composted,” Sorenson explains. “It’s then sold back to the farming co-op as a nutrient-rich soil supplement.”

Recently, Dulce Vida announced the launch of the Lone Star Edition añejo tequila, aged in Texas straight bourbon whiskey barrels from Hye, Texas-based Garrison Brothers Distillery. The barrel aging brings added levels of flavor complexity not common in tequilas. It retails for about \$75.

“I think in 10 years you’re going to see the rise of craft tequila products,” Sorenson predicts. “There are lots of them now and it’s very competitive; there will be a shake out. There are 10 or so that I know of just in Texas and surrounding states and we’re probably rising to the top of that pile or close to the top.”

And, he says, he’s amassed more than 25 gold medals from various tasting competitions to back that up. —J.C.



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analogy to craft brewing and they'd say, "Oh, I get it, you're small." Fast-forward seven years and most of Philadelphia's distributor partners have separate divisions or at least separate selling teams devoted to craft. That's another aspect in which recent changes in the spirits distribution landscape mirror the evolution on the beer-wholesaling side of the beverage alcohol business.

"[Distributors] are realizing that [craft spirits] may not be paying the bills today, but some of these brands are going to be the big brands of the future," Auwerda asserts. "I think they kind of wised up to how craft brewing's been over the past five years. They've given [craft spirits] more attention than they were and a more professional look at it."

The folks at Maine Distilleries, makers of Cold River vodka, have experienced a similar transformation with their distributor partners. That company formed in 2003, experimented for a couple of years and produced its first batch of what would become Cold River in 2005. Since then, there's been a marked shift in the amount of attention its wholesalers have been paying to Maine's brands. The distributors really started to change their tune when they began to realize that the small distillery wasn't going to be a flash in the pan.

"We'd gone with a couple of large distributors that treated us fine, but really didn't pay attention to us until we were around for a while—until they knew we were serious and had some staying power," remembers Chris Dowe, CEO of Maine Distilleries. "We always had a good product, but it took a full five years for these distributors to really pay attention and really start talking to their sales force, even though we were visiting them every month and going to their meetings."

On the opposite coast, Click Wholesale Distributing, headquartered in Kent, Wash., has made a name for itself over the past decade distributing craft beer and fine wine throughout Washington State. On March 1, 2012 it added spirits

CRAFT CLOSE-UP: Philadelphia Distilling Spirits of '76

When Philadelphia Distilling bought its still in 2005, it had its sights set on what the founders believed was an underserved segment of the spirits category: gin.

"At the time there weren't a whole lot of them," says co-founder Andrew Auwerda of the City of Brotherly Love-based company's desire to launch what became Bluecoat American Gin. "We came out at about the same time that Hendricks did and before that it was Bombay Sapphire, which was sort

of the newest gin and was already 15 or 20 years old. And the vodka space was extremely crowded—not that it isn't now, but at the time it seemed there was a launch every week... We were just trying to zig when everybody else was zagging." Philadelphia also produces an absinthe, Vieux Carré. Most recently the company began rolling out its XXX line of moonshine-inspired whiskeys, including LiberTea, which, as the name suggests, infuses tea, as well as honey and lemon in the recipe, and Salted Caramel whiskey.

"We thought we would do something different instead of a traditional strawberry, blueberry or peach, like they do in South Carolina, North Carolina and Virginia," Auwerda says. "We kind of went with our own Northeast take on, it. Salted caramel, at least for me [evokes] the Jersey Shore, taffy and carnivals—that sort of feeling." —J.C.



CRAFT CLOSE-UP: Maine Distilleries Spirited Spuds

Chris Dowe has a bone to pick with conventional wisdom.

"Everybody talks about vodka not having any flavor or any smell," he says. "Anyone who drinks vodka knows that every vodka has a flavor and every vodka has a smell."

As CEO, managing partner and head distiller of Freeport, Maine-based Maine Distilleries, Dowe should know. His company is responsible for Cold River vodka, distilled from potatoes grown in Maine. About a

decade ago one of the company's other partners, Donnie Thibodeau, a potato farmer, came up with the idea of using some of his state's starchy bounty to produce a distinct vodka.

The company went through a couple years of experimentation before it came up with the right formulation for Cold River vodka about seven years ago. Since then it has added a blueberry vodka—made from Maine-grown blueberries—as well as a traditional gin.

"We're in 15 states with full listings and then we're in six or seven states with partial listings—partial meaning that if there's a bar or restaurant that wants it, they can order it through the state and we'll ship it to them," says Dowe.

But its strength lies in its home region. "Our theme is Maine," notes Dowe. "One of the things we've always stressed is that we're adding value to Maine potatoes." —J.C.



Photo Credit: Claire Houston

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to its product mix. That was the first day it was legal for a private company to distribute distilled spirits in Washington after voters last November approved privatization in the erstwhile control state. In fact, at 9 a.m. that day, Click became the first company since the repeal of Prohibition to be able to legally do so. And since the state is a hotbed of activity for craft distilling activity—as well as craft beer and fine wine—Click has taken on a fair number of artisanal spirits brands.

“[Craft distilling] is growing very rapidly,” observes Click president and co-owner Rick Steckler. “We see a lot of similarities to craft beer from quite a while ago, maybe 15 or so years ago, where there are fledgling craft distillers who are very passionate, very creative, finding their way in the world of beverage sales.”

At last count there were a total of about 60 distilleries either currently operating or about to open in his state.

Steckler says he’s witnessed a wide range of quality and marketing knowhow among startup spirits producers. “[There are] some that really don’t appear to have a good grasp on it and others that, right out of the gate, are very good at it,” he offers.

However, one clear distinction Steckler sees between micro-brewed beer and micro-distilled spirits is that the latter require a stronger consumer and retailer education effort. “I think it’s going to be a bit of a bigger learning curve to get consumers to switch over from what’s so ingrained and what they’re used to on the spirits side—their call brand or favorite brand, or they’re not even thinking of spirits as being branded as much, whereas there’s a high degree of interest in craft beer, who or what’s behind the brand. When a patron walks into a bar, they look at the tap handle selection, they look at the list and they really want to try the new, cool stuff with brands that have really been making some waves. With spirits, we’ve got a longer road to get to that point, but it’s happening.”

Riding the Tailwind

With all of the momentum behind craft

spirits in 2012, what’s the market going to look like in, say, 2017 or 2022? If the market continues on its current trajectory, is it possible that craft distilling could be as much of a force within the spirits world that craft brewing is today—approximately 6 percent of volume and climbing—in the context of the broader beer market. “Not necessarily,” says BMC’s Sudano. “The biggest difference,” Sudano points out, “is that spirits core brands, the big ones, are still growing.”

Jack Daniel’s, for instance, still posts year-on-year volume gains, as does Smirnoff, albeit largely from flavor extensions. The same can’t be said for beer, where macro premium domestics like Budweiser and Miller Lite continue on downward trajectories.

“The large branded products in spirits are still growing,” Sudano notes. “You don’t see that in beer. That’s why you see the acceleration in the fragmentation of beer because they’re taking it out of the major brands. You don’t see that yet in spirits. But on a macro basis, the characteristics are very similar. So I would expect [craft spirits] to continue to grow.”

There certainly will be considerably more players over the next several years. It’s no great stretch of the imagination to anticipate a distillery census that numbers in the quadruple digits before the current decade is over. “There are 5,000 cities in America,” says ADI’s Owens. “If one in five cities could have a small distillery in it, we could get to 1,000.”

And despite all of the very obvious comparisons that have been made with craft brewing, Owens is confident that there’s one aspect that will be different for craft distilleries. He points to his own experience as a former brewery owner—Buffalo Bill’s Brewery.

“When I had my brewery back in the ’80s, a lot of people started up and a lot of people failed,” he remembers. “I’ve been doing ADI for 10 years and I think I’ve only seen four people go out of business. It’s not people saying let’s start a distillery and see what happens. It’s peo-

ple who have a strong commitment to the idea and to the money. They put their money where their mouth is and they’re in it for the long haul. [These] people have it in their DNA.” **BW**

The Top-Shelf Look

In addition to attracting the attention of consumers and distributors, the momentum the craft spirits segment has been enjoying also has caught the eye of suppliers to the industry, which have been developing solutions tailored to the burgeoning artisanal movement. Glass packaging producer O-I, for example, recently unveiled the Imperial, the latest addition to its Specialty Stock Bottle portfolio, which it’s marketing to crafts to house their high-end products.

Imperial features a broad-shouldered frame, which O-I says is designed to command a top-shelf presence. Its wide label panel, O-I adds, allows a high degree of customization of a range of labeling techniques, enabling greater differentiation opportunities for craft spirits brands.

The bottle made its North American debut in September, after being part of the successful launch of Ron Marques del Valle rum in South America last year. —J.C.

