Route to Market and Marketing

Navigating regulatory system constraints

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TO PARAPHRASE DICKENS, it is the best of times and the worst of times.

Getting an alcohol product to market in the U.S. has never been so easy, or so hard. While today's marketing and social media technology is sophisticated and easy to use, this is countered by a regulatory and distribution system designed for a different era. The restrictions are real and are increasingly frustrating small and large industry members alike.

From the international brand that can't get products to U.S. audiences that have sampled the product in the foreign country, to the medium size producer that celebrates getting signed up by a distributor only to find the brand buried in a product book the size of the Manhattan phone directory, the U.S. market punishes any new market entrant who does not understand the system. The methods to overcome the worst of the impediments require capital, expertise and, most important, patience.

The Best of Times – Products Have Never Been Better or More Varied

We exist in a time of unparalleled technological competence. Almost every new product on the market, including imports from international producers utilizing the latest production technology, are well made from high quality ingredients and produced in state of the art facilities. Building a market for a superior new product (wine, spirits or beer) starts with a good marketing and product introduction plan. Marketing plans will reside within a system that does not reward creativity; at least insofar as using new techniques to capture market attention is concerned. This confuses and frustrates new entrants in the market.

The Test Market

Every well-designed plan starts with a test market. It could be one or more cities, states or regions. The size of the test market is determined by the financial resources of the producer, the product available for the chosen markets and personnel resources available to guide the product introduction process.

The first market restriction is the reality that regulatory and event regulations, taxes, import requirements and distributor rights vary state by state. There have been many good products that failed out of the gate because the producer introduced them into too many new markets at once and couldn't keep up with the management burden of understanding the unique nature of each new market. Compounding the dilemma, there are not only unique regulatory requirements in the individual state markets but often unique local market regulatory requirements.

The Purpose of the Test Market – Creating Brand Ambassadors

Events and sampling events are the best way to build a core consumer base. Wineries (and, increasingly, craft distillers and craft breweries) have a built-in advantage with an attractive physical plant usually in a tourist friendly urban or rural area, the availability of tours and the marketing savvy to turn visiting customers into brand ambassadors. If the producers story and approach works in the test market expansion to other markets, once the larger market regulatory nuances attributable to the specific product category are understood and observed, can be undertaken on a market by market basis.

Foreign producers are at a disadvantage because they must introduce their products through local retailers, which requires navigating the three-tier system from the outset. There must be a national importer, a state or regional wholesaler and a local retailer willing to carry the product. Running that gauntlet is an issue for the creative producer because it must be accomplished without unlawfully inducing the retailer to carry the product; all the while still using the inefficient three tier distribution system.

What Can Go Wrong with Marketing to Retailers and Consumers?

The major regulatory inhibition throughout the U.S. is the prohibition on giving away anything for free to a customer, or anything of value to a retail account. Free goods and "things of value" are easy for the regulators to understand, and crack down on.

From sponsorships of music events held at premises where the event promoters have an interest (such as in the 17 **BottleRock ABC** accusations, where wineries were suspended for 10 days or forced to defend their sponsorships in expensive and time consuming hearings) to advertising that your brand will be available at a specific retailers' location (unless its more than one), to providing retailers with a monthly stipend for tap handle availability (the **MA Distributor Craft Brewers Guild** case, where the producer was fined $2.6 million, to limiting Point of sale (POS) to those accounts that buy the brand supplying the POS (in the NV Harrah's cases, the **TTB** collected approximately $1.9 million in fines), to providing dozens of retailers with televisions, draught equipment and coolers (the **California ABI** accusations involved a $200,000 fine doubled if the settlement terms are violated, staff training to prevent pay-to-play prohibitions, and the cessation of similar incentive programs).

These are all examples of "thing of value" violations that could have been prosecuted by either (or sometimes both) state or federal enforcement officials in any state.

The point is often made (usually by us when defending a case) that at some level everything that is used to induce sales is a "thing of value." The regulatory response is "get an exemption" if you want to give anything away, be it a product or a service or (recently in California) even an in-store coupon.

It is the exceptions that the producers must know about in each market. Too often even distributors in the state either did not know about, or deliberately ignore because of a lack of enforcement, the regulations in their own state. That is why homework on the intended market is imperative. Making sure that marketing plan is cleared by a competent alcohol marketing professional in the local market is a basic requirement.

Successful Marketing

Once the plan is in place the next steps are to decide what routes to market are available to the specific producer and the specific product.

For the domestic winery, the best answer is to aggressively implement a direct-to-consumer (DTC) sales program revolving around events at the winery supported by presentations on the road where consumers can be sampled on the products and support for wine club programs strengthened. DTC should always be the focus of the domestic winery. It is the most valuable exemption in the system today.

For the international winery, or domestic craft distillery or brewery, three tier system programs can be designed around local restaurant programs, and (where permitted) around trade tastings and charitable events. However, few retailers have DTC rights beyond their own state for any product. This limits the development of any DTC program involving distilled spirits, beer or international products to those producers that use third party marketing web sites that coordinate national advertising with local retail product availability.

Successful Distribution

Expansion though on-premise is the key—if people haven't sampled the product they are unlikely to buy it, and consumer demand generates interest in the product from traditional retail sources. We advise selecting states where product can be provided without undue difficultly and to find small distributors willing to commit to the product– we often find that large distributors require producers to do their own marketing and end up as just very expensive product clearing services.

Making a good hire for state and national sales management is essential. In a family business, this can be a member of the family. Consumers react favorably to a story told well by a person with a stake in developing the product.

What Can Go Wrong?

Three-tier system costs are always a concern—distributor margins up to 40% for just a delivery service can be a killer, as are long term distributor agreements that provide no exit if distributor failure occurs. Franchise state laws are another trap that can lock up brands so be careful who you partner with in franchise states—many distributors make more money out of franchise exit fees than they do out of selling the product. Finally, always retain DTC and private label/control label (PL/CL) rights in any distribution agreement.

The Road Less Taken – PL/CL

Where there is an opportunity for direct retailer contact by a domestic or international producer always look for the opportunity (where permitted by the state) to place a special product in that account. It can be a "control label" where the intellectual property is owned by the producer but the specific brand is dedicated to the individual retailer. It can also be a true private label where the intellectual property is owned by the retailer. The positive side to this approach is that distribution margins (which can go as high 40 percent in some markets) are reduced to a more palatable level consistent with distribution costs. This is also a good way to build up the name of the producer in the retail channel involved (on-premises or off-premises) and is a good outlet for excess volume. These relationships need not be large volumes. The most important element is retail relationship itself.

Conclusion – Be Smart, Plan and Be Strategic

We all know that alcohol is a heavily regulated product. How its regulated is the key to finding a path through the thicket of different federal, state and local regulations, and through the three-tier system. The value proposition must always be based on the price and quality of the product, and not on free goods or "things of value" used to induce purchases either at the consumer or the retail level.

It all starts with a plan, and with good management choices. **WBM**