



DEVELOPING PRINCIPLES FOR  
REGULATION OF  
**ALCOHOLIC BEVERAGES**  
SECTOR IN INDIA

EXECUTIVE SUMMARY

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## EXECUTIVE SUMMARY

The global alcoholic beverages market was estimated to be at USD1.58 trillion in 2020 and is projected to grow at a compound annual growth rate (CAGR) of around 3.5 per cent between 2020 and 2023. India is one of the fastest growing alcoholic beverages markets globally, with an estimated market size of USD52.5 billion in 2020 and the market is expected to grow at a CAGR of 6.8 per cent between 2020 and 2023. According to the Ministry of Food Processing Industries, production of alcoholic beverages in the country increased by about 23.8 per cent during the period between 2015-16 and 2018-19. The alcoholic beverages industry contributes to around 1.5 million jobs in India and generated around USD48.8 billion in sales revenue in 2019. The sector is open to foreign investments and many states offer subsidies for local manufacturing (for example, Maharashtra and Karnataka for wines). From the demand side, factors such as rapid urbanisation, changing consumer preferences and a sizeable and growing middle-class population with increased purchasing power have contributed towards growth in demand for alcoholic beverages. According to industry estimates, the number of people consuming alcohol increased from approximately 219 million in 2005 to 293 million in 2018; it is projected to increase to 386 million by 2030. The share of the upper-middle income group in alcohol consumption has increased steadily from 7 per cent to 21 per cent and is expected to increase to 44 per cent by 2030.

Alcoholic beverages are among the top three sources of revenue earning across most states. Yet there seems to be a lack of transparency, predictability, and clarity in the tax regime to ensure that the revenue earning objective is aligned with other objectives of the government like 'Make in India' and exports from India. The governance and pricing models for alcoholic beverages vary widely across the states. The states through their excise policies, control the entire supply chain of alcoholic beverages from manufacturing and distribution to registration and retail. There are frequent and ad-hoc changes in these policies, creating uncertainty and preventing manufacturers/ distillers to plan their investment.

Given this background, this report, based on secondary information analysis and a primary survey, provides an overview of the Indian alcoholic beverages market, highlighting market trends and contributions of the sector to the economy. It specifically examines the regulatory and pricing related policies across select states and their impact on the industry, its supply chain, quality of products available to consumers and consequent effects on health. Specifically, it examines the different models followed by states such as corporation model, wholesale model, direct model and distribution model and their impact on designing an efficient supply chain. It examines whether price control measures have been successful in achieving the desired objectives, namely (a) higher revenue earnings and (b) consumer protection. The

report also shows how policies and excise duties have been sporadically changed during the recent coronavirus (COVID-19) pandemic.

*This report then makes policy recommendations on how state governments can learn from global best practices and customise them to the requirements of their respective states to develop a predictable and transparent pricing model that will enable the government to meet its objectives of earning higher revenue, address consumer health and safety concerns, increase investment in manufacturing in line with the 'Make in India' initiative, create employment, bring in foreign direct investment and increase exports.*

## 1. Key Findings

### Global Trends

Since 2010, more than 78 countries have imposed price controls on alcoholic beverages through an increase in excise

taxes to protect consumer health. However, alcohol consumption globally, and in India, is price inelastic, which implies that higher prices may not deter consumption. Therefore, governments through the right policies can guide consumers towards lower intake and higher quality consumption. Citing examples of regulations from a number of countries, the report points out that such regulations should be designed through extensive data modelling and in a transparent manner. This would protect consumers' health and at the same time would enable the governments to earn revenue and facilitate exports.

### Changing Consumption Trends

The report highlights some interesting market trends. While consumption of spirits dominates the Indian market, its share in volume terms has decreased from 55.02 per cent to 50.31 per cent during 2013-2018 (see Figure A). The share of beer consumption has increased from 44.56 per cent to 49.25 per cent while that of wine has remained almost constant between 0.42 and 0.50 per

Figure A

### Consumption of Alcoholic Beverages in India by Product Categories



Source: Compiled from International Wines and Spirits Record (IWSR) 2018. Domestic Volume Report. All Categories India.

cent. The primary survey shows that over 70 per cent of the growth in alcoholic beverages consumption in India in the next decade will be driven by the lower middle and upper middle-income groups, and there is a growing trend towards product premiumisation. Premium products have recorded a five-year CAGR of 7.7 per cent in 2018, of which bottled imported spirits recorded a CAGR of 10.9 per cent. By 2030, 50 per cent of consumers are expected to buy more of the same category of alcoholic beverages that they were consuming, 26 per cent are estimated to move to higher brands, and 24 per cent are expected to spend on newer categories of alcoholic beverages.

### International Trade

India is a small player in global alcoholic beverages trade. In 2019, India's total share in global exports of alcoholic beverages was only 0.27 per cent, with a global rank

of 32, much below a number of developing countries. In the same year, India's share in global imports was 0.75 per cent with a rank of 20. India has an export potential in this sector, which can be addressed through measures like tariff reduction and ensuring transparency in regulations across states to support manufacturing and "Make in India".

### State Revenues from Alcoholic Beverages

An analysis of the receipts from state excise across 10 states studied in this report show that in the year 2017-18, the share of revenue from alcoholic beverages varies across states, but it is among the top three revenue earning components for all the states. In 2017-18, the share of revenue from alcohol was close to 99 per cent of the total revenue in majority of the 10 states considered for the study; the exceptions were Madhya Pradesh and Rajasthan, which had a share of 77 per cent and 94 per cent, respectively (see Figure B).

Figure B

### Share of Alcoholic Beverages in the Revenue Collection of 10 States (Excluding Petroleum) - 2017-18



Source: State Budgets 2019-20.

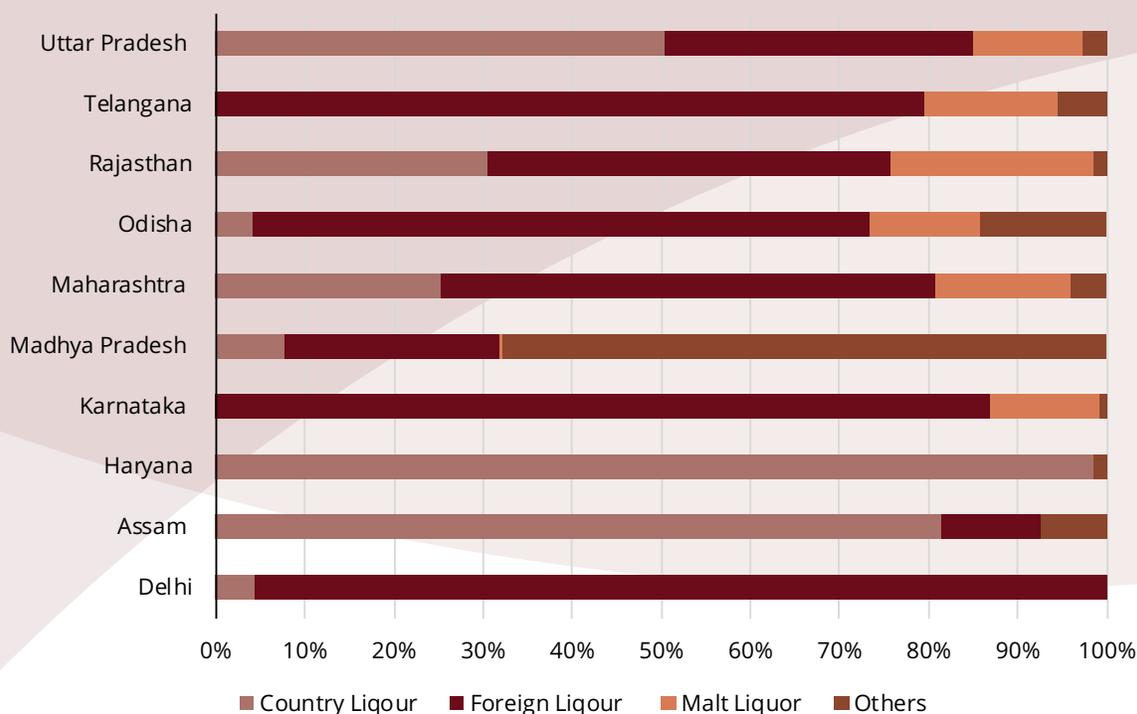
In terms of revenue collection, between 2013-14 and 2017-18, Telangana had the highest CAGR of 30.39 per cent, followed by Odisha (12.92 per cent) and Assam (12.69 per cent). Lowest CAGR was recorded in Maharashtra (6.29 per cent). However, in both 2013-14 and 2017-18, Karnataka and Maharashtra had the highest shares in revenue collection from alcoholic beverages sector among the select 10 states.

Revenue by product categories (see Figure C) show that in 2017-18, in states such as Delhi (95.55 per cent), Karnataka (86.98 per cent), Telangana (79.61 per cent), Odisha (69.18 per cent), and Maharashtra (55.50 per cent), the highest revenue was earned under the 'foreign liquors and spirits' category. In states such as Haryana and Assam, the highest

revenue earning was from the 'country spirits' segment with a share of 98.51 per cent and 81.31 per cent, respectively. In Uttar Pradesh and Rajasthan, revenue earnings from both 'foreign liquors and spirits' and 'country spirits' were almost equal, with a combined share of 84.93 per cent and 75.6 per cent, respectively of total revenue from alcohol. In Madhya Pradesh, the highest revenue collection (67.76 per cent) was from 'other receipts' segment and not from alcoholic beverages, per se.

The northern states such as Haryana and Punjab ensure the receipt of 80 per cent of their projected revenues at the start of the financial year through a system of lottery/ auction of wholesale and retail licence and, once a certain number of licences are

Figure C  
Revenue by Product Categories Across Select 10 States (2017-18)



Source: Compiled and calculated by authors from the respective state budgets of 2019-20.

granted for that year, the government is assured of revenue in the form of licence fees irrespective of the actual sale of liquor by licensees. In such cases, revenue gets assured even during the recent COVID-19 related lockdowns. In some states, the tax burden is on manufacturers while in others like Delhi, the tax burden is passed on to the consumers which may lead to a shift towards consumption of lower quality products.

### *COVID-19 Related Ad-hoc Tax Increases: Leading to Revenue Losses*

During the COVID-19 pandemic, around 21 states have increased excise duties, additional excise duties, maximum retail price (MRP), bottling fees, and imposed COVID-19 specific fees, cess and surcharges to avoid revenue shortfall and meet consumer health needs. Out of the 10 selected states in the report, 8 have imposed such taxes and fees, exceptions being Maharashtra and Madhya Pradesh. In states such as Assam, Rajasthan, Karnataka and Uttar Pradesh, changes were brought in through hike in excise duty slabs; while in states such as Delhi, Haryana, Odisha and Telangana, specific COVID-19 related cess/fees were implemented. The impact on final prices of the products ranged between 5-25 per cent; except in Delhi, where prices increased by 70 per cent initially due to imposing of a special corona fee of the same percentage.

As per industry estimates during the survey, between March and September 2020, pan-India sales volumes were lower by 25-30 per cent. Consequently, revenue earnings were lower; specifically, Delhi had a loss in revenue of around 25 per cent, while it was around 40-45 per cent in Odisha. The higher taxes led to lower revenue collections, which eventually prompted the states to readjust the taxes and some states started to offer sales through online channels. This exemplifies the need for

a nuanced evidence-based and transparent planning process for this sector.

### *Route-to-Market Channels*

States decide the channels for alcoholic beverages sales through their excise policies. Majorly, there are four types of distribution channels across states – (a) distributor model (company> distributor> retail) in states such as Maharashtra and Assam; (b) corporation model (company>corporation>retail) in states such as Rajasthan, Karnataka, Madhya Pradesh and Tamil Nadu; (c) wholesale model (company>wholesale>retail) in states such as Haryana; and (d) direct model (company>retail) in states such as Delhi.

Prior to the pandemic, only in-premise sales were allowed but during the COVID-19 pandemic, home delivery and e-commerce channels have been allowed in some states such as Odisha and Delhi.

## **2. Key Barriers**

### *• Regulatory Barriers: Variations Across States*

The survey found wide variations across states in terms of their policies and implementation. Some states lay down new or updated excise policies every year (generally during the beginning of the fiscal year); in some states, excise policies may not be revised for many years, including no variations in the prices approved for manufacturing companies or suppliers. In some states, excise policies may not be available online and, if available, may not be updated or may not be available in English, making it difficult for businesses to read and interpret. From the selected 10 states, in Haryana, Maharashtra, and Odisha, the policies are available in English and for the past five years; in Assam, Delhi, Karnataka, and Telangana, the policies are available in

English but cannot be accessed online for the past five years; and in Madhya Pradesh, Rajasthan, and Uttar Pradesh, the policies are not accessible in English but are available for the past five years.

Examples of policies taken from 10 states in this report shows that different state policies, and regulations create differences in pricing models, cost structure and taxes, governance models, route-to-market channels and setting up of businesses. Among the 10 identified states, in 2020, the lead time taken to issue licences was highest for Maharashtra (minimum 45 days) and Karnataka (40-45 days). The lowest lead time was recorded for Uttar Pradesh at 7 working days, in spite of the licences being issued manually. In Assam, the registration and licence issuing processes is online but, the lead time was recorded at 20 days in the year 2019-2020. Such measures reduce ease of doing business and dilutes the basic premise of 'Digital India'. It converts India into more than 30 heterogeneous markets instead of a single market. The state level variations are also likely to be raised by India's trading partners like the Australia, European Union and the United Kingdom during trade agreement negotiations.

#### • *Price Control Barriers*

The alcoholic beverages sector is kept out of the ambit of the goods and services tax (GST) regime, and as such the state governments have the freedom to implement their independent price control mechanisms, based on their priorities. This creates variation in the pricing models and methodologies applied across states. In case of calculating the ex-distillery price (EDP) or final price of the products, for whisky, the process of fixing EDP differs across states. In Haryana, Uttar Pradesh and Rajasthan, lowest EDP among the neighbouring states

and in Madhya Pradesh, lowest EDP across India is taken into account; in Karnataka, Maharashtra and Assam, a free pricing policy is executed; in Telangana, EDP is determined through open tender; and in Delhi, a combination of lowest EDP and free pricing is followed, based on the price of the product.

Price control is one of the core components of regulating the sector, and variation in taxes and consequently in final prices of products encourages illegal trade from neighbouring states. Additionally, variation in definitions/terminologies for final price of products creates barriers for businesses.

The survey highlighted that most states fix their EDPs for whisky based on the lowest EDP among the neighbouring states, and they do not consider differences in production costs across states. Further, the EDPs are not revised periodically, ignoring the inflationary pressures. In all, the pricing mechanism is non-transparent due to lack of evidence-based data-driven policy making.

#### • *High Import Tariffs*

High import tariffs and cess of 150 per cent, even for intermediate products, counters the basic premise of "Make in India". While imports will not be more than one percent of the domestic consumption even if tariffs are phased out, imported liquor prices in India are significantly higher than 95 per cent of the countries in the world and India's trading partners have repeatedly raised this as a key barrier in their trade agreement negotiations.

### 3. Impact of the Regulations and Pricing Mechanism

The survey showed that variation and sporadic regulations have (a) often led to decrease in or significant loss of potential revenue for state governments (b) led to the growth of illicit liquor market and death

related to its consumption (c) increased the requirements of multiple permits and compliance burden for the manufacturers, reduced ease of doing business and, (d) forced consumers to shift to lower quality products leading to health hazards. Due to excessive monitoring, policing and control over the supply chain of products from manufacturers to retailers, not many players have come up in this sector, resulting in an oligopolistic structure. Only around 30 per cent of the logistics companies undertake transportation of alcoholic beverages. The sector has low value-addition and high dependence on imports. And, in spite of the willingness of the industry, India has not been able to develop its manufacturing capabilities and export to its potential in this sector, due to regulatory complexities. Survey participants pointed out that India will not be able to sign trade agreements with key trading partners like the United States, European Union, United Kingdom or Australia, if it continues with high tariffs and cess and state level non-tariff barriers.

Further, the survey found that the unpredictable nature of the state excise policies and the variations in the timing of their release adversely affects production cycles of manufacturers/companies operating across multiple states. The states have not been able to achieve their desired objective of collecting tax revenues due to the ad-hoc nature of implementing policy changes, as has been the case of imposing taxes during COVID-19 in some states. Further, the policy changes are often not substantiated by detailed analysis of sectoral data trends, undermining evidence-based policymaking. At a country level, India has not been able to become a leading exporter unlike China or Chile, in spite of having significant potential and in spite of subsidies offered by Centre and states for select alcoholic beverages

production, due to complicated state level policies.

#### 4. The Way Forward

The report prescribes five-point policy recommendations towards developing transparent and predictable regulatory and pricing principles for the alcoholic beverages sector. These are as follows -

- *Adopt Clear and Predictable Policies:* The state excise departments should lay down clear policies at predictable intervals of two to three years, which can help businesses to expand, to make long-term investments, and encourage new business models to flourish. To encourage transparency, the excise departments should focus on adopting a 'cost-based' EDP formula over the 'minimum EDP' criteria and evaluate the impact of changes in pricing across various categories of beverages (like premium, standard, etc.) for effectiveness of taxation policy. This report highlights some core principles of developing a model taxation policy, which are based on best practices adopted globally and in India. Such a model can help the state governments to meet their objectives of higher revenue, consumer health protection and addressing the issue of tax leakages and illicit markets. The tax slabs need to be revised periodically in line with inflation and changes in prices of raw materials. Greater transparency and predictability would encourage entrant of new players and competition.
- *Technology Interventions:* The state excise departments need to switch to digital methods of granting licences and permits, which can prevent

unaccounted transactions and corrupt practices. Data analytics and technology-based solutions need to be adopted by the states to monitor the supply chain and develop front-to-back traceability. Specifically, physical monitoring should be replaced by technology driven tracking and tracing initiatives to monitor transportation of products from the manufacturer to the distributor to the retailer. This can be especially helpful in case of inter-state movement, where there are chances of illegal sourcing of liquor.

- *Develop Data-Driven Models:* To achieve the desired policy objectives (such as protecting consumer health or enhancing state revenues) and to enhance transparency, evidence-based pricing and taxation models should be developed by states based on detailed research and longitudinal production and consumption data analysis. There is a need to invest in collecting structured and periodic data on household consumption patterns (by age, social indicators, area, type of alcohol, etc.) and the impact of price increase or other policy changes on consumption patterns. In this regard, state governments can refer to global best practices for implementing such models. This report has highlighted how an effective model can be designed.
- *Conduct Regular Consultations:* State excise commissioners, finance ministers, and other stakeholders should engage in regular in-depth discussions to start off a process of transparent, predictable and consultation-based price

determination. To begin with, such consultations can be held at the level of individual states and on demonstrable metrics being met, a bigger group of states can come together in identifying uniform principles of taxation and to set the stage to develop a transparent and uniform model pricing framework. The states should also consult and provide inputs to national-level agencies such as the Department of Consumer Affairs, in helping them to establish definitional uniformity regarding maximum retail price (MRP)/ maximum or minimum selling price (MSP) of products.

- *Phased Tariff Reduction and Exports:* The government should focus on phased tariff and other duties reduction and Indian companies should be encouraged to export to improve the trade balance. Duty reduction for intermediate products can enhance value addition in India and boost domestic manufacturing potential. Duty reduction above a threshold level will only allow entry of high-end produce, which do not compete with domestic production.

In conclusion, if the recommendations of this paper are implemented, it can help the state governments in meeting the objectives of earning higher revenue, addressing consumer health concerns, and creating employment. Adoption of technology can enable removal of irregularities along the entire supply chain, with limited government intervention. The recommendations can help India in bringing in more investments into the sector, encourage innovation, improve ease of doing business, increase domestic manufacturing capabilities and enhance exports.

India is one of the fastest growing markets for alcoholic beverages. Various factors including a sizeable middle-class population with increased purchasing power, rapid urbanisation, changing consumer preferences, and reduction in cultural barriers to drinking, have contributed towards growth in demand for alcoholic beverages. Revenues from taxation of sales in this sector are among the top-three revenue earning sectors for the state governments and the sector generates significant direct and indirect employment.

The states through their excise policies, control the entire supply chain of alcoholic beverages from manufacturing and distribution to registration and licensing processes, labelling and packaging requirements, and retail. Price control is one of the core components through which the states regulate this sector. However, the pricing policies and governance models vary across states, creating different route-to-market channels. There are frequent and ad-hoc changes in policies, creating uncertainty and deterring manufacturers/distillers to plan their businesses in advance. The variations in regulations and operating models across states have added to the compliance burden of participants across the supply chain, leading to low ease of doing business. It has resulted in India becoming a fragmented market, undermining the concept of India as a single market. Further, unlike other countries such as Chile, India has not been able to leverage its export potential in this sector, in spite of having potential.

Given this background, this report, based on secondary information analysis and a primary survey provides an overview of the Indian alcoholic beverages market, highlighting market trends and contributions to the economy, the supply chain and the various routes-to-market followed across states. The report outlines the regulatory framework governing the sector, both at the centre and across states; and presents the changes effected in the regulations, sales channels and duties, among others, with the onset of the COVID-19 pandemic. The report is a first of its kind, which specifically examines regulatory and pricing related barriers and their impact on the industry, its supply chain, quality of products available to consumers and consequent effects on health, states, and the Indian economy as a whole.

The aim of the report is to help the state governments to develop regulations based on certain principles which makes the regulations predictable and transparent. The report suggests the way forward on how the state governments can learn from global best practices in creating uniformity in developing their pricing models, building transparency and creating more predictable policy environment through data driven and evidence-based policymaking. If the recommendations of this paper are implemented, it can help the state governments in meeting the objectives of earning higher revenue, addressing consumer health concerns, and creating employment. The recommendations can help India in bringing in more investments in to the sector, encourage innovation, improve ease of doing business, enable "Make in India", enhance exports and the country can be a key player in global value chains of alcoholic beverages.



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