

The U.S. Craft Distilling Market: 2011 and Beyond¹

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This paper surveys the existing U.S. Craft Distillers, segmenting the market geographically, by product category, and by entry-type. It also analyzes growth trends in the Craft Distilling market to date, and compares those both to market resurgences in similar businesses (U.S. Farm Wineries and U.S. Craft Breweries), and to the broader history of the U.S. Distilling industry.

1. Introduction

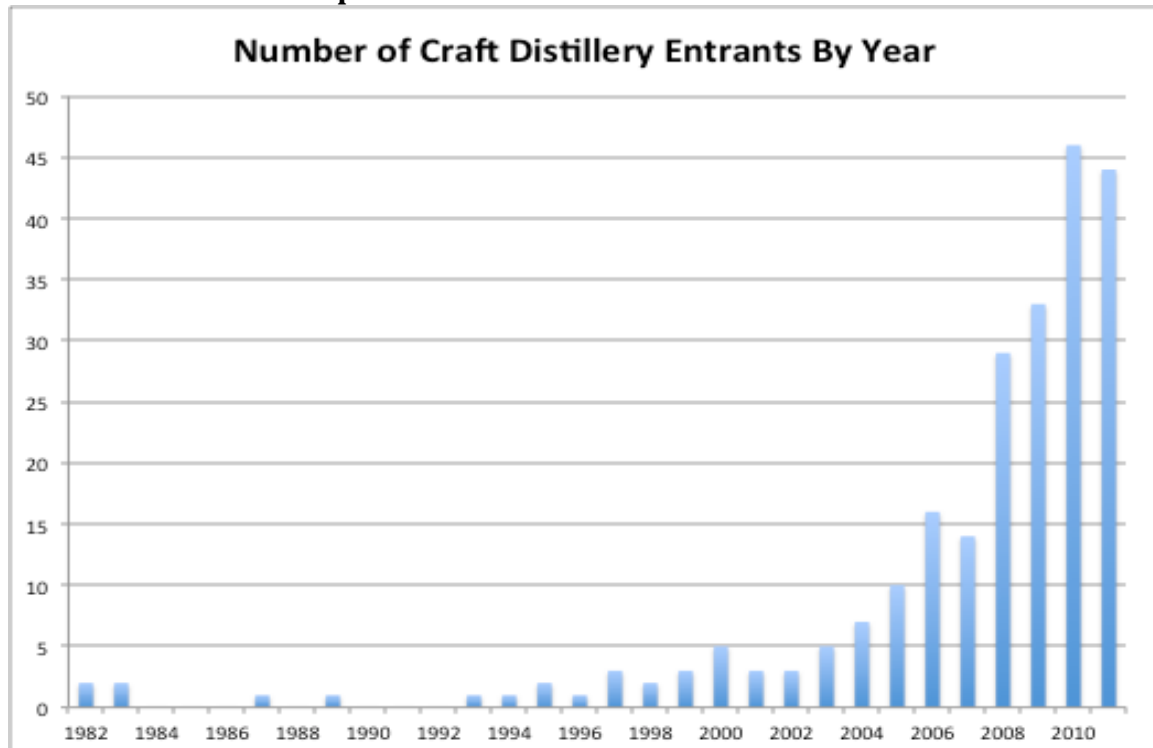
The Craft Distillery industry in the United States is undergoing explosive growth right now. The number of identifiable Craft Distilleries in production has gone from 24 in 2000, to 52 in 2005, to 234 at year-end 2011, and new entrants are showing up with regularity. Often consolidation to a few large firms in an industry creates opportunities for new, smaller entrants to fill market niches and reach customers the large producers cannot². The U.S. Craft distilling market fits this pattern well.

This paper will trace the growth of the U.S. Craft Distillers, provide summary statistics on the current market entrants, and put the ongoing Craft Distillery resurgence in the historical context of the distilling industry in the United States. Should the Craft Distilling industry continue along its current growth trajectory, the number of firms in the market will likely grow to more than 1,000 over the next 10 years.

2. Craft Distilleries By Entry Year

The Craft Distilling industry in the United States began in California in 1982 with the entry of two firms, Germain-Robin and Jaxon Keys Winery (also known as Jepson Spirits). The following year St. George Spirits and Domaine Charbay, also both in California, joined them. As can be seen in the following chart, the number of new entrants was very low in the industry's early years, often with no entrants at all.

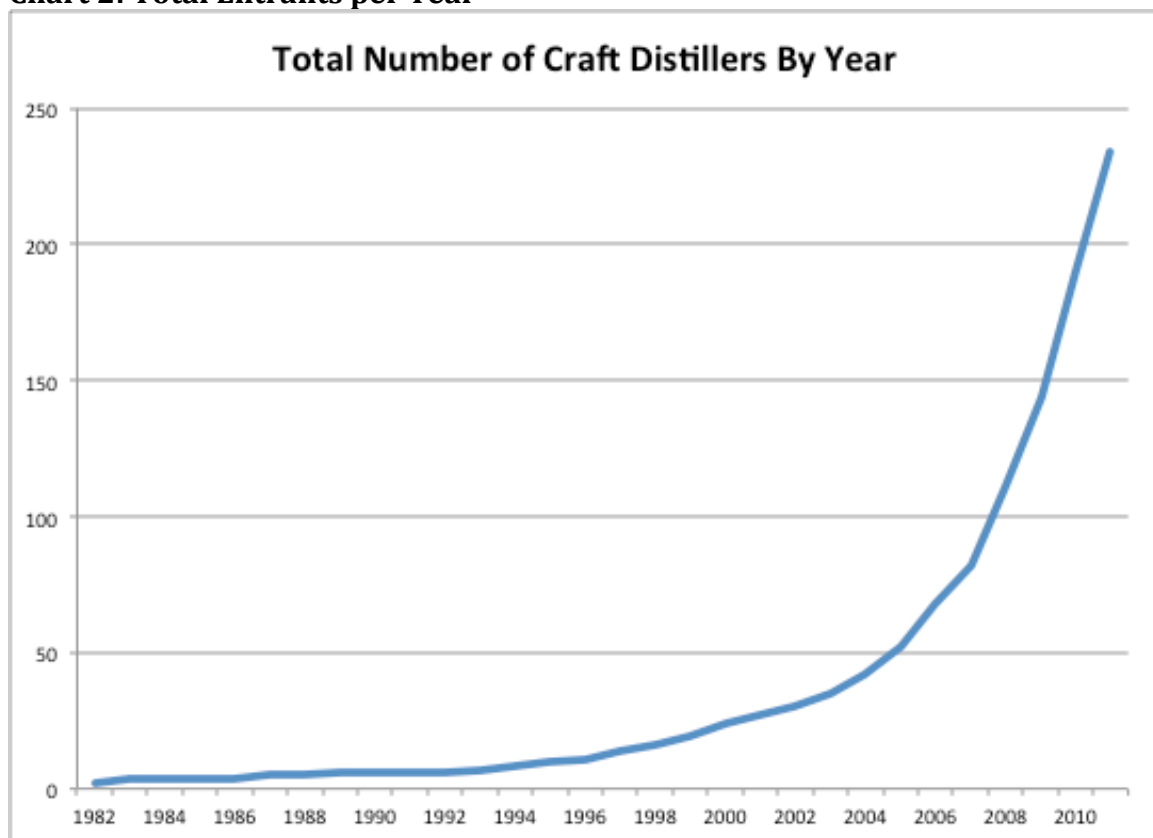
Chart 1: New Entrants per Year



This is also a common feature of new industries, as the “industry form” strives for recognition as a unique, distinct class of companies. As the form becomes more widely recognized, new entrants have a template and an identity to model. Often, there is a geographic component in the emergence of new industry forms, and the state-level regulatory issues in distilled spirits give this particular salience. It is no accident that the first four firms are all based within a hundred miles of each other in Northern California, one of the epicenters of the “Food Revolution” of the 1970s, and the founding place of the U.S. Craft Brewing industry 20 years prior (Anchor Steam).

The number of annual Craft Distillery *entrants* is still growing at a nearly exponential pace. The 2011 number is almost certainly low due to “hidden entrants” not in the available data sources, and the likely true number of 2011 entrants is closer to 55. When all the entrants by year are put together, we see the number of total market participants (Chart 2) also showing exponential growth.

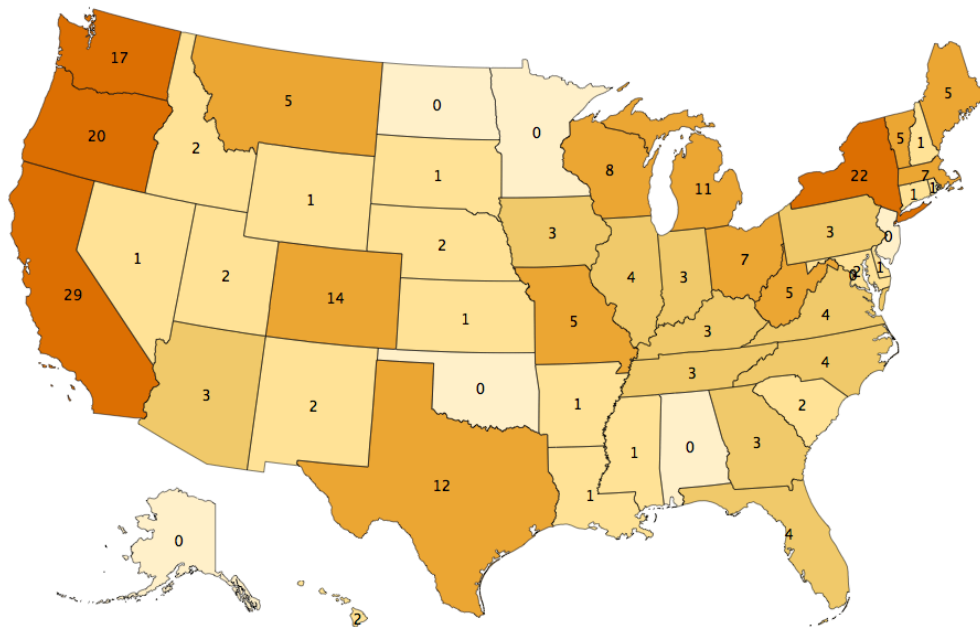
Chart 2: Total Entrants per Year



3. Craft Distilleries By State

As mentioned above, markets often display a geographical component, with many entrants clustered in a particular geography, or entrants in one place influencing or impelling entrants in a nearby geography³. In the case of the U.S. Craft Distillers, state-level differences in licensing requirements may lead to a profusion of entrants in one state, and few or none in a state next door. Generally, the entry of the first Craft Distillery in a state has lead quickly to more, and, although not the subject of this paper, favorable changes in licensing requirements have been “trigger events” in individual states. For example, in New York, where my firm, Coppersea Distilling, is setting up, the passage of the Farm Distillery Act in 2007 made it significantly easier to establish a distillery, and the number of New York Craft Distillers went from 5 in 2007 to over 20 in 2011. Below (Chart 3) is the distribution of entrants by state as-of 2011.

Chart 3: Operating Craft Distilleries By State, 2011



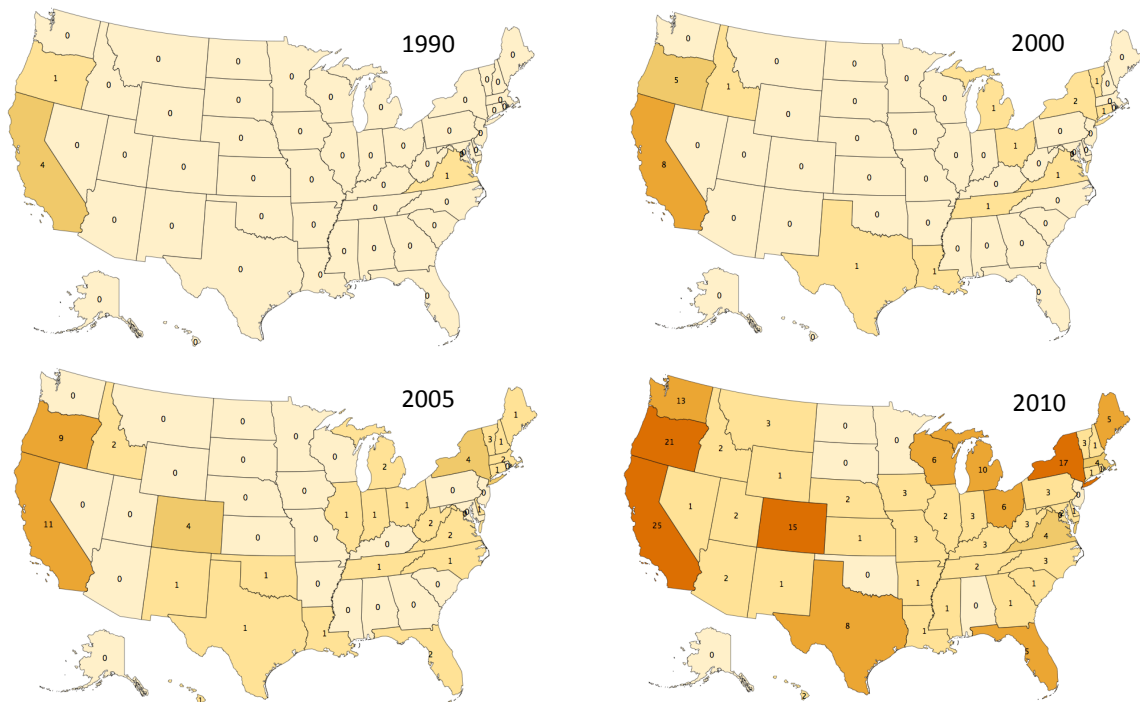
California, the state of first entry, continues to be a leader in the market, as do the nearby states of Oregon and Washington. Oregon was the 2nd state with a Craft Distillery, Clear Creek, which opened in 1987; and the strong “handmade” and “locavore” culture in the Pacific Northwest have proven fertile grounds for starting businesses such as Craft Distilleries. Washington’s market has grown from its initial entrant in 2007 to 17 in 2011. Other notable states include Texas, where Tito’s Vodka (1997) was the sole entrant until 2007 and now has company. Colorado’s market has grown smartly with Peach Street, Stranahan’s and Leopold Brothers

making an early mark. Tuthilltown, while not the first entrant in New York (several winery-distillers predate it) has been instrumental in lobbying for Farm Distillers, resulting in a raft of new entrants. The upper Midwest states of Wisconsin, Michigan, and Ohio feature strongly as well.

Also notable is the lagging behind of the Southern & Trans-Appalachian states considered to have strong roots in folk distilling (“moonshining”). The reasons are many, but certainly the number of folk distillers making spirits with traditional methods as handed down orally for generations is vanishingly small, and now dwarfed by the number of urban and sub-urban hobbyists bootstrapping their way with 10-gallon stove-top stills. However, now that many of these states have gone from none to one to three or four entrants, I would expect their numbers to continue to grow as they have elsewhere.

The bigger story, as seen in the progression in Chart 4 is that in 2000 only 12 states had operating Craft Distilleries; today Craft Distilleries are operating in *45 states*, making this a truly national phenomenon.

Chart 4: Operating Craft Distilleries By State, 1990-



4. Craft Distilleries By Product Type & Entry Path

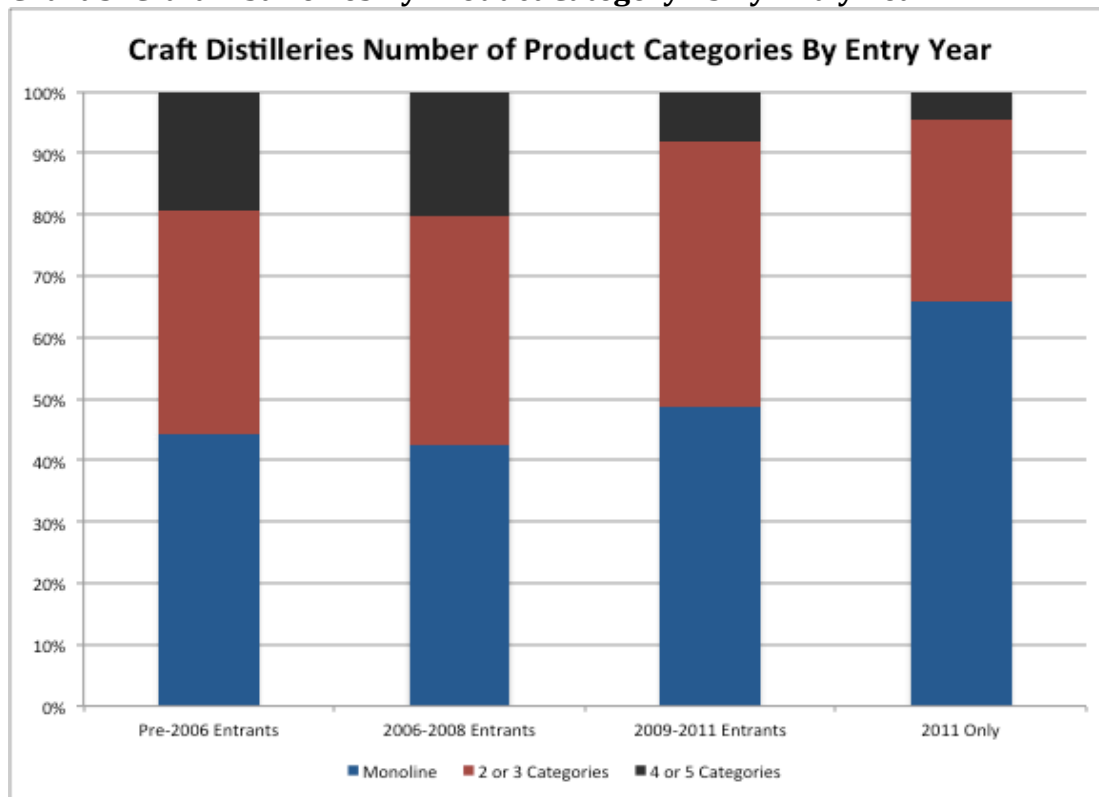
Craft Distillers are making an incredible variety of distilled spirits products. For the purposes of this analysis, I segmented the market into five major product categories:

Vodka, Gin, Whiskey, Rum, and Brandy/Other; this last includes Eau de Vies, Cordials, Liqueurs, and a profusion of unique, specialist products.

Indeed, one of the aspects of an industry revival is the emergence of specialized producers amidst the flowering of new entrants. Included in these are Craft Distilleries offering products such as Limoncello (HelloCello, CA), Asian-Pear-based Eau de Vies (Subarashii Kudamono, PA), and Arak & Ouzo (Bear and Eagle Products, CA). Even traditional categories, such as Vodka, are seeing not just, for example, organic producers (of which there are several), but also unusual sources such as a honey-based product (“Bee Vodka” from Hidden Marsh, NY).

While there are generalist entrants such as Leopold Brothers in Colorado or Triple Eight in Massachusetts with products across all five categories, almost half (46%) of the current entrants are single-category firms (see Chart 5). Another 40% are making products in 2 or 3 categories with the remaining 14% producing a wider range of products. This summary, however, obscures the underlying trend, which is that more of the newer entrants are single-category (“Monoline”) firms. In fact, two of every three of the 2011 entrants were single-category entrants, but as these firms mature some will also move into multiple categories.

Chart 5: Craft Distilleries By Product Category #s By Entry Year

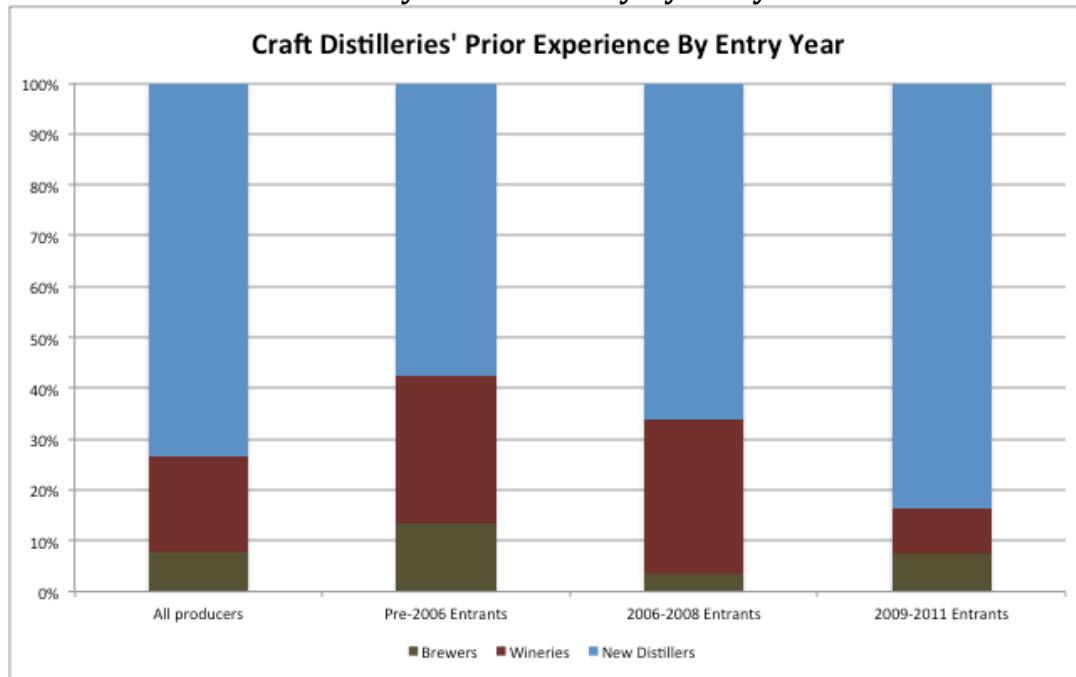


Many Craft Distillers make Vodka: it is easy and straightforward to make, requires no aging, and remains the single largest spirits category by case-volumes. More than

half of Craft Distilleries are producing and selling Vodka, and this percentage is consistent across entry years. About 30% of all Craft Distilleries produce Gin. Also un-aged, but with more opportunities for the distiller to impart unique flavor profiles, Gin has seen a slight decline over time in the *percentage* of Craft Distillers devoting energy to this category. Of course, the *number* of Craft Distillers making Gin has almost trebled since 2006.

Rum has held fairly steady as a product category through time, with about 25% of Craft Distilleries in this category. Brandy/Other has shown the largest changes, with the percentage of Craft Distillers in the category falling off sharply in recent years. This is actually a secondary effect of a change in the composition of the entrants (see Chart 6). The early entrants in the Craft Distilling industry tended towards Brandy & Eau de Vies, partly because proportionally more of them were Wineries. Of the 111 entrants through 2008, 33 (about 30%) were also Wineries; since 2009 only 11 of the 123 entrants shared that trait, a drop to less than 10%.

Chart 6: Craft Distilleries By Prior Industry By Entry Year



Whiskey has undergone a revival of its own in recent years, and amongst the Craft Distilleries, Whiskey has jumped to become the single most popular category of products amongst the more recent entrants with 52% shipping a product in this category.

Chart 7a: Craft Distilleries By Product Category By Entry Year (Number)

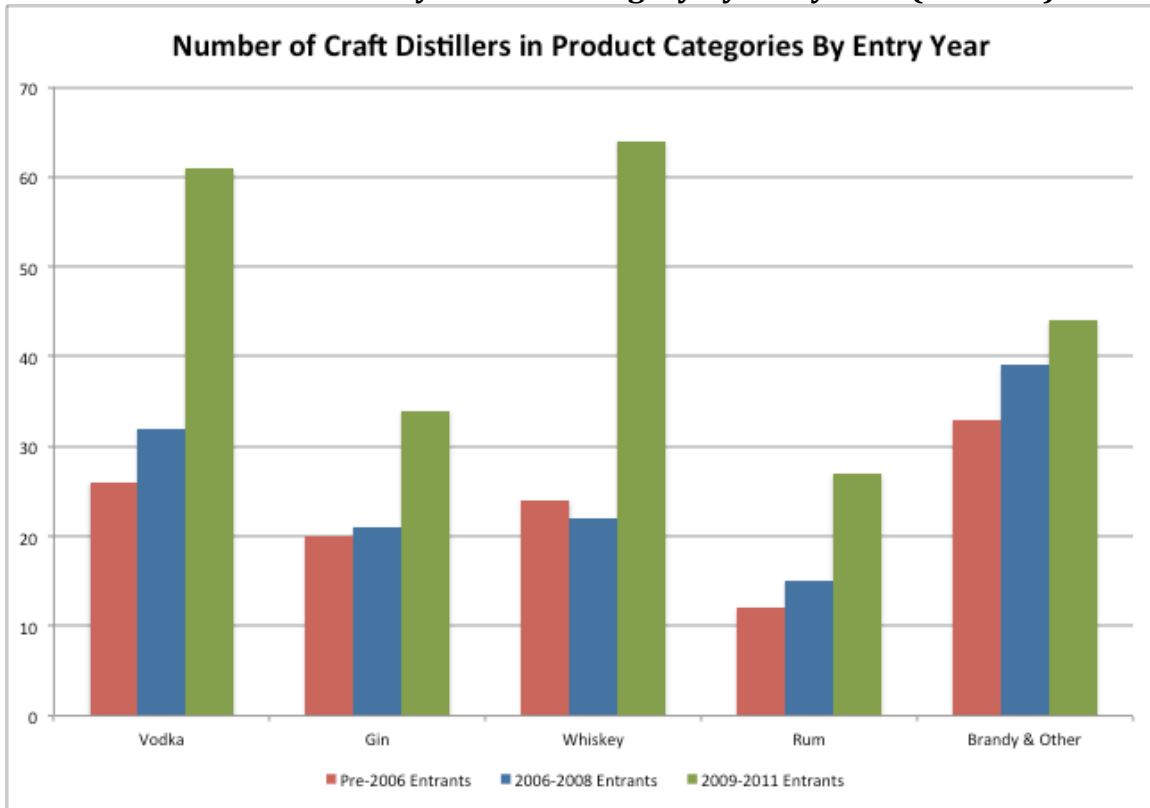
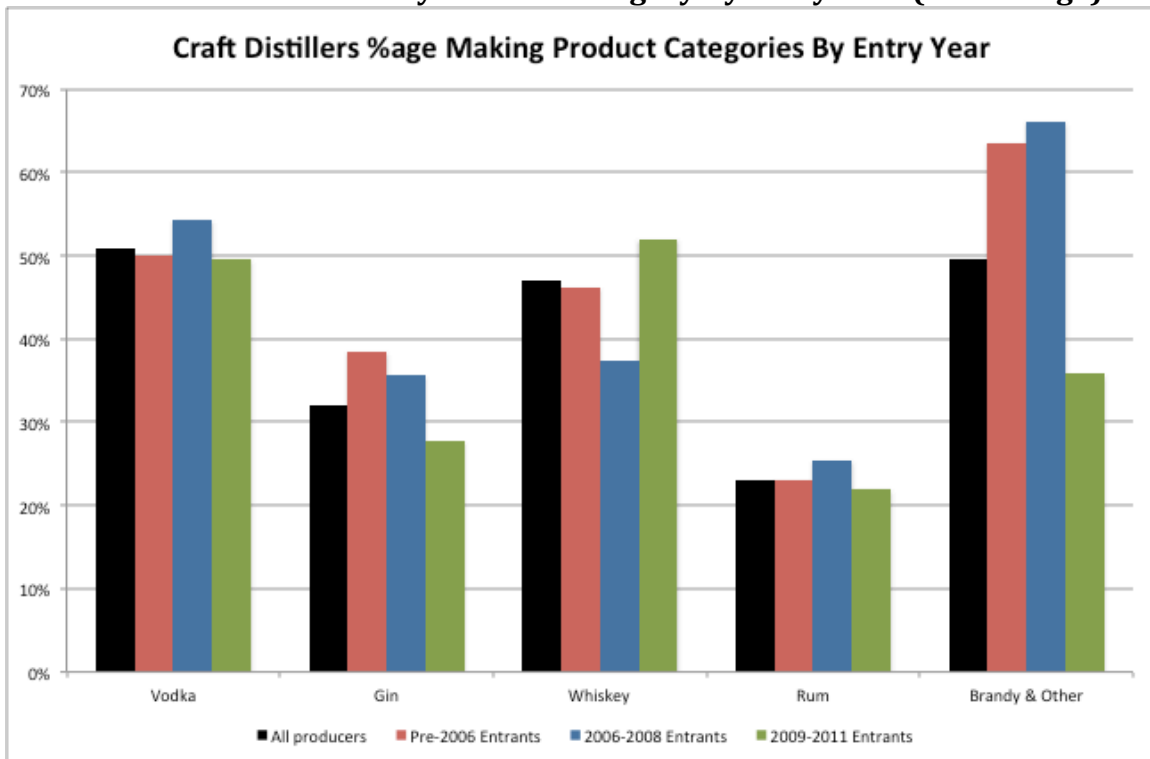


Chart 7b: Craft Distilleries By Product Category By Entry Year (Percentage)



5. Growth Trends in Craft Distilleries; Comparisons to American Distilling History, Farm Wineries, and Craft Brewers; and Predictions for the Future

This history of American distilling is no small subchapter of American economic, industrial, and social history, but is tightly woven right into the fabric. The Whiskey Rebellion, the molasses Rum-distillery portion of the “triangle passage,” and, of course, two Constitutional Amendments and the grand social experiment known as Prohibition are all part of any general history of the United States.

This distilling history includes well-kept statistics on the number of distilleries in the country. As the charts (Charts 8a & 8b) below show, in the late-19th Century, the number of (legal) distilleries in the United States was well into the thousands, and, prior to the adoption of the Coffey still after the 1830s, was in the *tens of thousands*.⁴ As was true across a range of industries, the spread of mass marketing, national transportation networks, industrialization, and urbanization led to consolidation. Thus the smaller producers were being marginalized and saw their numbers shrinking even well before Prohibition virtually destroyed the small distillery market in the United States.

Chart 8a shows the total number of licensed distilleries in the U.S. for the past 130 years. Prior to WWI, that number was over 1,000. Even immediately after Prohibition, there were several hundred distilleries, a number that would decline to fewer than 100 in the early 1980s, when the U.S. Craft Distillery market was in its infancy.

Chart 8a: Number of U.S. Distilleries, 1880-

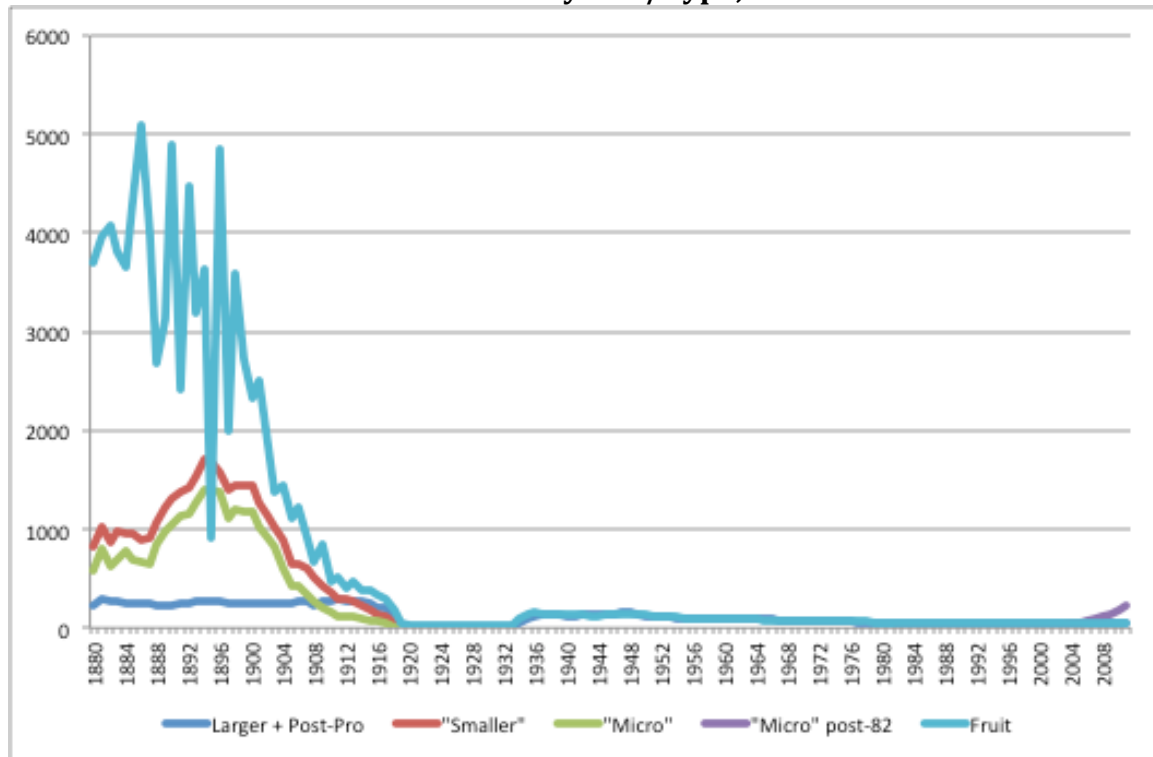


The total number of distilleries in the late-19th Century obscures the significant distinctions in the market. The Treasury Department gathered statistics on operations, warehousing, deposits and withdrawals from warehouses, and the like. The primary distinction amongst distilleries was between Grain (“Registered” distilleries), Fruit distilleries, and Molasses distilleries. For all of this history, the number of Grain and Fruit distilleries remains roughly equal (there are scarcely a dozen Molasses distilleries in any given year).

The secondary distinction, within the Grain distilleries, is by production size. The IRS Commissioners’ reports to Congress for the years prior to Prohibition dutifully report on the number of “Larger” and “Smaller” distilleries annually. Further analysis reveals that the distinction is based on the number of bushels used daily, and that the “Larger” category includes 60-100 bushels/day, 100-500, and 500+, while the “Smaller” category includes distilleries in usage ranges of <5 bushels/day, 5-10, 10-20, 20-40, and 40-60.

And still more review uncovers *yet another* size category of producers, defined not in bushels/day, but as having “Daily Spirit Capacity Not Exceeding 30 Gallons,” and whose numbers are not reported at all in the “headline” pages of the Commissioners’ reports. Presumably these producers went unreported because, although quite significant in numbers, they were a very small part of total production and, hence, revenue. I have called these producers the “Micro” category, reserving “Craft” distilleries for the post-1982 resurgence.

Chart 8b: Number of U.S. Distilleries By Size/Type, 1880-

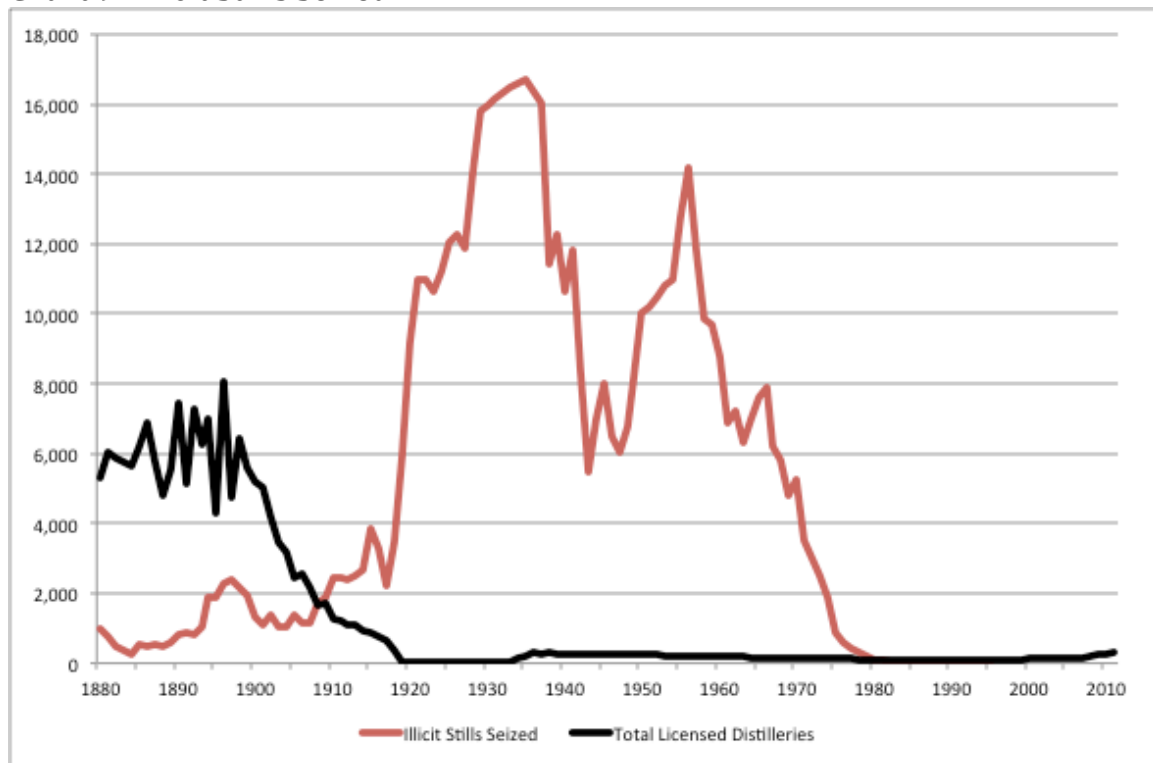


The extraordinary volatility in the number of Fruit distilleries could be a function of harvest conditions in individual years, although that is a guess on my part. What is more certain is that, post-Prohibition, California and Kentucky host a large majority of the few remaining Fruit and Grain distilleries, respectively, and that the number gradually declines amidst consolidation across the spirits industry to a very few number of very large players: Diageo, Beam, LMVH, Pernod-Ricard, Brown-Forman, Grant & Co., etc.

Of course, these charts only account for the legally licensed distilleries in the United States. Because alcohol taxes were such an important part of Federal Government revenue pre-Prohibition, the IRS took very serious steps to crack down on “Illicit Distilling.” The popular image of the “Appalachian holler” moonshiner, evading government revenuers to either a) practice his long-cherished family craft without interference, and/or b) make some un-taxable cash income was no accident.

Pre-Prohibition the number of “Illicit Stills Seized” (Chart 9) gradually rose in response to the ongoing economic squeeze on small producers by bigger players, the broad forces of Temperance, and also specifically as a result of the economic depressions of 1893 and 1907. Even so, the number of Illegal producers increased by an order of magnitude during Prohibition, declined following Repeal, then shot back up in the 1950s, only to tail off gradually into the 1980s until, from 1990-1995 the total number of Illicit Stills Seized is **two**. Even so, the difference in scale is quite striking following Prohibition.

Chart 9: Illicit Stills Seized



Part of this phenomenon is certainly a result of changing enforcement priorities. By the 1980s, with the number of Illicit Stills being found declining, and cocaine, amphetamines, and other drugs emerging as a larger social issue, there were undoubtedly fewer officers looking for illegal distilling operations. But, I believe, more of this decline is due to the demographics of the moonshining community itself, and broader trends in American folk traditions and their legacies.

Someone actively “moonshining” during Prohibition would’ve been about 20 years old in 1930, or born about 1910 (when life expectancy itself was only 50 years). By 1970, our moonshiner is 60 years old, and by 1990 he’s blowing out 80 candles on his cake and probably not moonshining anymore.

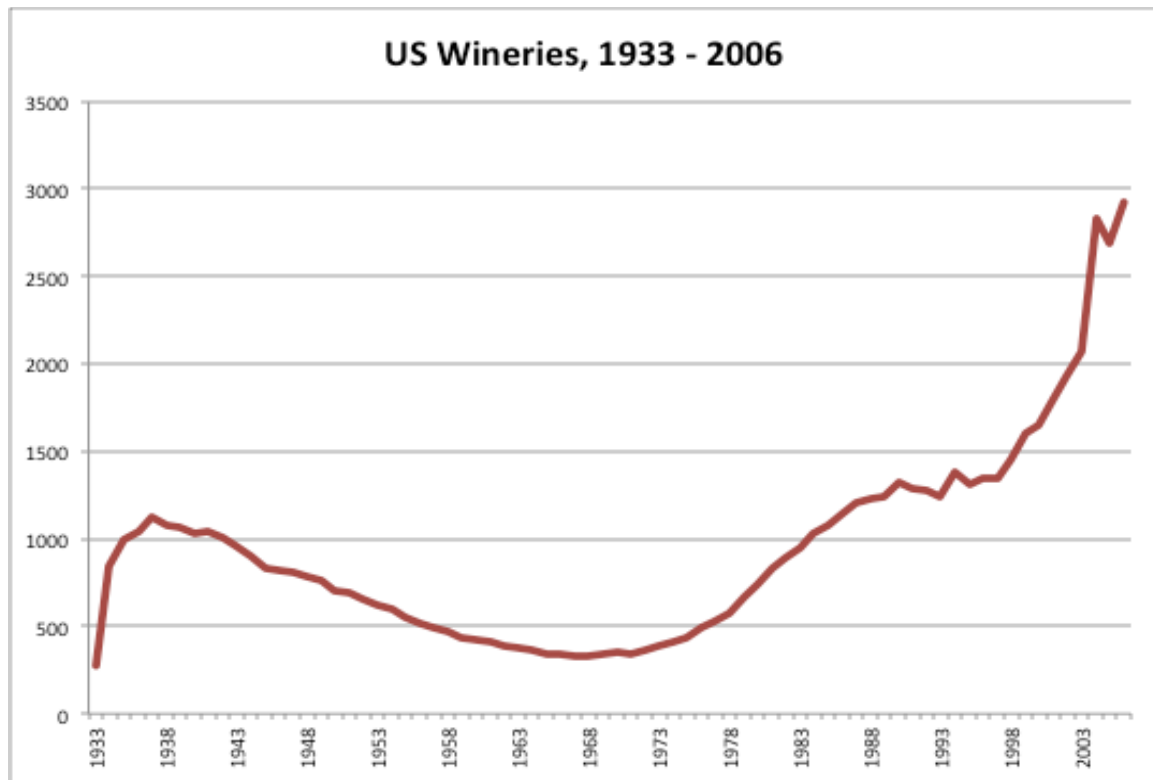
The aging, and passing, of the Prohibition generation of moonshiners in the 1960s-80s also coincided with the urbanization and sub-urbanization of the rural South alongside a wave of non-Southern immigrants, both from the Northern U.S. and from abroad. These cultural shifts affected the practice and transmission of traditional Southern folk arts⁵, resulting in a significant decline in the number of folk distillers who would have learned the craft from family through an oral (and physical) transmission process. Simply put, the number of traditional folk distillers in the United States still regularly operating by the early 1980s had fallen to a fraction of what it was only a generation prior.

Thus, when the U.S. Craft distilling market begins in the early 1980s, the number of distilleries, legal and illegal, in operation in the United States was almost certainly at an all-time low. From the dawn of the Republic, when stills could be found across the country on many farms and in virtually every village, to the late 19th Century when small-scale distilleries operated, to the Prohibition-world of illegal operations, the number of stills in operation in the U.S. has been measured in thousands, if not tens-of-thousands. And in 1980, there were **fewer than 100** registered distilleries and only **106 Illicit Stills** found.

There has been ample precedent in which consolidation of previously diffuse industries to a very small number of generalist players leads to a resurgence of specialized entrants to exploit market niches. While researchers have observed this phenomenon in industries as diverse as Airlines and Savings and Loans⁶, two particular examples resonate with the U.S. Craft Distilling market, namely the U.S. Farm Winery market, and the U.S. Craft Brewery market.

In a 1995 paper,⁷ Anand Swaminathan, Goizueta Chair & Professor of Organizations and Management at the Goizueta Business School at Emory University, noted that the number Wineries in the U.S. declined from over 1000 in 1940 to a low of 330 in 1967; the corresponding numbers for Farm Wineries were over 700 and 141, respectively. What followed was gradual growth in the Farm Winery segment from 1970-1990 back to those 1940 numbers, a leveling off, and then, subsequent to the paper’s publishing, another spurt upwards in entrants.

Chart 10: Number of U.S. Wineries 1933-2006



Professor Swaminathan also researched the U.S. Brewery industry, along with Professor Glenn Carroll, Laurence W Lane Professor of Organizations at the Graduate School of Business at Stanford University. They looked at the U.S. Brewery industry⁸ from its founding event in 1633 through the reemergence of the Craft Brewers in the 1990s (Chart 11).

Beyond the sheer impressiveness of their data set, there are a number of amazing facts. First is that the number never goes to zero—there has been at least one Brewer in operation in the U.S. since the initial founding event. Second is that while Prohibition shows up plainly on the chart, the exponential decay process that is pushing the number of Brewers from over 2000 to fewer than 50 is well underway before Prohibition and continues almost “to a T” thereafter. Finally, the speed with which the number has shot back up to nearly 2000 firms rivals the post-1850 market transformation brought on by the massive German and Irish immigration of the period.

Chart 11: Number of U.S. Brewing Firms, 1633-



Looking at the Wineries, Brewers, and Distilleries together since 1880 (Chart 12a) offers a “wide scale” view of how these markets have evolved over time. The view is suggestive of a 20-year lag between the rebirth of the Wineries, Brewers, and, now, Distillers, but that could be more coincidence than causal. What seems more apparent is that the number of Distilleries in the United States is returning to more historically “normal” levels, and that Distilled Spirits consumers, like Beer and Wine consumers before them, are turning to more hand-crafted, smaller scale producers for a variety of taste and perceptual reasons.

Finally, when we compare the number of Craft Distiller entrants with the number of Craft Brewers using the industry founding date as a “reference clock,” (Chart 12b) we see an uncanny similarity. While there are naturally differences in the markets, I believe the resurgence of Craft Distilleries in the United States is still in the early innings.

Chart 12a: Distilleries, Brewers, and Wineries, 1880-

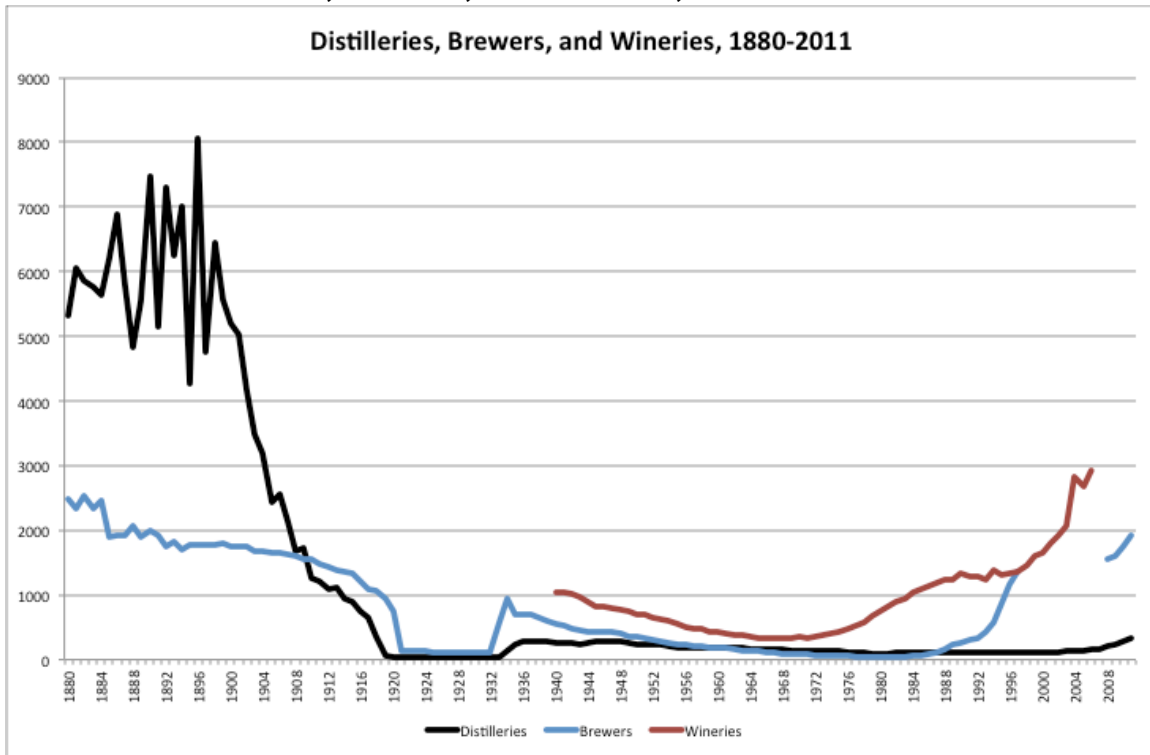
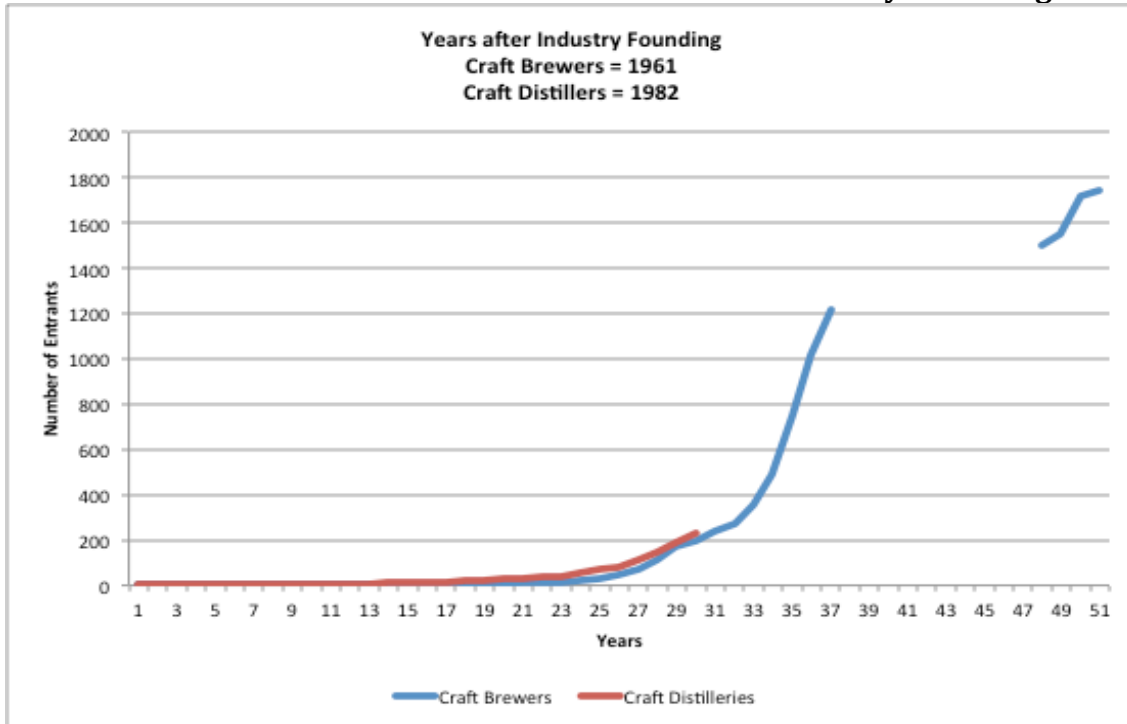


Chart 12b: Craft Distilleries and Craft Brewers From Industry-Founding Date



6. Conclusion

The number of Craft Distilleries in the U.S. will grow to over 1000 within the next 10 years. The Craft Distillery market is following closely the models of the Farm Winery and Craft Brewery markets in which specialist producers making unique products transformed the industry.

Craft Distillers are thriving in both traditional product categories, such as Vodka, Gin, and Rum, as well as introducing new product ideas, such as the emergent trend in “White Whiskey,” sold with very minimal barrel aging. Craft Distillers have opened facilities across the country and brought a renewed regional vigor to spirits production.

The emergence of Craft Distillers as a recognized form, along with favorable changes in legislation, have led to the profusion of entrants in recent years, and these are just the “leading edge” of a return to the highly diffuse market structures as seen in the past.

7. Notes & Acknowledgments

¹ Data & Sources. I am grateful to several individuals for providing guidance and access to data. Bill Owens of the American Distilling Institute made the ADI's annual Directories, from 2006-2012 available. Data on the Craft Distilling industry comes primarily from my personal research and analysis of the names contained in those directories.

Anand Swaminathan and Glenn Carroll graciously shared the longitudinal data on the Wineries and Brewers. They are working to fill the gaps in the Brewers data from 1998-2007 and in the Wineries from 2007-fwd.

Data on U.S. distilleries and "Illicit Stills Seized" comes from the annual IRS Commissioners Reports to Congress (available online in their entirety), and the annual Spirit's trade compendium "The Liquor Handbook", initially published by Gavin-Jobson (1956-84), then by Jobson Publishing Corp. (1985-95), and now by Adams Media, Inc. (1996-fwd). Data for "major" U.S. Distilleries from 1994-fwd is estimated pending response from the TTB.

² For a general introduction to these issues, see Carroll, Glenn R. and Hannan, Michael T., 2000, The Demography of Corporations and Industries, Princeton University Press. In particular, Chapter 12, "Segregating Processes," discusses environmental conditions and founding rates of specialist organizations.

³ See, for example, Carroll and Hannan, 2000, Chapter 9, "Organizational Environments", or Michael Porter, 1998, "Clusters and the New Economics of Competition," Harvard Business Review, Nov. 1998.

⁴ Rorabaugh, W.J., 1979, The Alcoholic Republic, Oxford University Press, p.87. "The number of distilleries in the entire country rose from 14,000 in 1810 to 20,000 in 1830 and then fell to half that number a decade later." Table 3.2 on the same page shows the number of distilleries in New York falling from over 1100 in the 1820s to 77 in 1860.

⁵ Various "moonshine reminiscences"-type books have drawn this conclusion regarding the decline in both number and quality of Southern folk distilled spirits. See, for example: Jerry L. Alexander's Where Have All Our Moonshiners Gone?, James Earl Danby's Mountain Spirits, Esther Kellner's Moonshine Its History and Folklore, and even more recent works such as Max Watman's Chasing the White Dog. None dare provide firm statistics on how many folk distillers are or were in operation.

See also: Burrison, John A., 2007, Roots of a Region: Southern Folk Culture, University of Mississippi Press. Prof. Burrison describes the general trends in Southern folk traditions, both their challenges and sustaining characteristics. In a personal exchange, he also hypothesizes that many of the moonshiners may have shifted to marijuana production and other illicit activities with higher profits.

⁶ See Carroll and Hannan, 2000, Chapter 12.2 'Empirical Research on Partitioning' for further references.

⁷ Swaminathan, Anand, "The Proliferation of Specialist Organizations in the American Wine Industry 1941-1990," *Administrative Science Qtly*, Vol 40 #4, Dec 95, pp 653-680.

⁸ Carroll, Glenn R and Swaminathan, Anand, 1991 "Density Dependent Organizational Evolution in the American Brewing Industry From 1975 to 1988," *Acta Sociologica*, Vol 34 #3, Jan 1991, pp. 155-75.

--, 1998, "Why the Microbrewery Movement? Organizational Dynamics of Resource Partitioning in the American Brewing Industry After Prohibition," *American Journal of Sociology*, Vol 106 #3, Nov 2000, pp. 715-762.

8. About the Author

Michael Kinstlick formally co-founded Coppersea Distilling, LLC with his partner, distiller Angus MacDonald, in 2010. His experience prior to Coppersea includes asset management, technology business development, commercial insurance, and structured finance. He has a BA in Economics from Columbia University, a MS in Industrial Engineering from Northwestern University, and an MBA from the Haas School of Business at UC Berkeley.