

Building a strategy to combat illicit trade in Kenya

Alcoholic Drinks

Executive Summary

Report compiled by Euromonitor International for Alcoholic Beverages Association of Kenya (ABAK)

June 2023

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The data included in this report is accurate according to Euromonitor International's market research database, at time of publication: June 2023

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Introduction

Who is Euromonitor International?



Making sense of global markets

Our market research solutions connect your organisation's goals with global opportunities.

Our services

- Syndicated market research
- Consulting

Expansive network

- 1,000+ on-the-ground researchers in 100 countries
- Complete view of the global marketplace
- Cross-comparable data across every market

Our expertise

- Consumer trends and lifestyles
- Companies and brands
- Product categories and distribution channels
- Production and supply chains
- Economics and forecasting
- Online pricing data

Illicit Trade specialisation

Comprehensive analysis of illicit trade issues impact clients and Governments and strategies to mitigate.

- **Expertise:** A dedicated team of experts engaging with public and private sector stakeholders on illicit trade including counterfeits, contraband, tax leakage, expired goods, homemade products.
- **Experience:** Analysis of the size and cost of illicit trade and supply chain issues across international markets and key sectors; alcoholic drinks, tobacco, pharmaceutical, beauty & personal care, packaged food.
- **Methodology:** Consistent definitions and research methods to support comparative market analysis.
- **Partnership:** Findings are used by global organizations and leading companies to increase awareness about illicit trade issues and implement feasible strategies to mitigate them.

How we help our clients



Industry Impact Analysis

- Identify the biggest markets and future drivers



Sizing and Regulatory Analysis

- Measure the market, its share, structure and regulatory framework



Mitigation Strategies

- Where to tackle in the supply-chain and policies designed for local success



Tracking Effectiveness

- Track the effectiveness of taxation or regulatory changes and consumer campaigns

Research Objectives

The Alcoholic Beverages Association of Kenya (ABAK) with its members would like to build knowledge and understand the drivers of the illicit alcoholic drinks trade, its shape, its size and impact on government revenue in Kenya.

To this end, what effective measures/strategies are required to tackle the issues to create longer-term solutions. ABAK wishes to help government to understand the size of the problem, as well as identify ways to combat this issue.

The project objectives include:

- Estimate the market volume, value, and fiscal loss attributed to illicit alcohol sales by sub-category.
- Segment the illicit alcohol sales by type of illicit activity.
- Identify and evaluate key hotspots of illicit alcohol activity across sub-categories and product brands.
- Understand the dynamics of illicit; trading, products, purpose, pricing and distribution, etc.
- Qualify the trends and drivers related to the illicit alcohol market.
- Identify consumer perception of illicit activity and government actions.
- Explore the current extent of knowledge of illicit alcohol within government.
- Develop and outline solutions that could help combat the trade of illicit alcohol.



Research methodology

Desk Research

1) In-house data analysis

- Legal alcoholic drinks data alignment.
- Legal market data and trends.
- Sizing of the illicit market.
- Estimation of fiscal loss.

2) Secondary research

- Official stats about production, imports, exports, seized illicit products and per capita consumption.
- Press articles, current tax structure and regulations, etc.

3) In-depth trade interviews

#15 in total

- Regulatory bodies, alcohol industry players, trade associations, supply chain actors, government agencies, etc.

4) Consumer survey

n=1,009

- Understanding of perception of illicit alcohol, channels where consumers believe these products are sold, perceptions of government actions, etc.

5) Informal store visits

#40 store visit observations
across various areas

- Observation exercise: prevalence of products, selling prices, key brands and product types, packaging, label information, selling conditions, pulse interviews with staff etc.

In-Country Research

Kenya



Source: Image from Britannica.com

Definitions

Category	Definition
Licit Alcohol	Alcoholic drinks that are legally tax compliant in terms of paying the correct excise and other duties as required by the country in which the beverages are sold.
Illicit Alcohol	The non-payment of relevant excise and other duties to be fully tax compliant. Illicit alcohol can also lack other official requirements within a specific market. Some of the most important requirements that may be lacking include necessary health permits, and compliance with the local laws and norms applicable to the alcoholic drinks production process, including ingredients.

Abbreviations: HL – Hectolitre, LAE – Litres of alcohol equivalent

Illicit Category definitions

Types of illicit alcohol

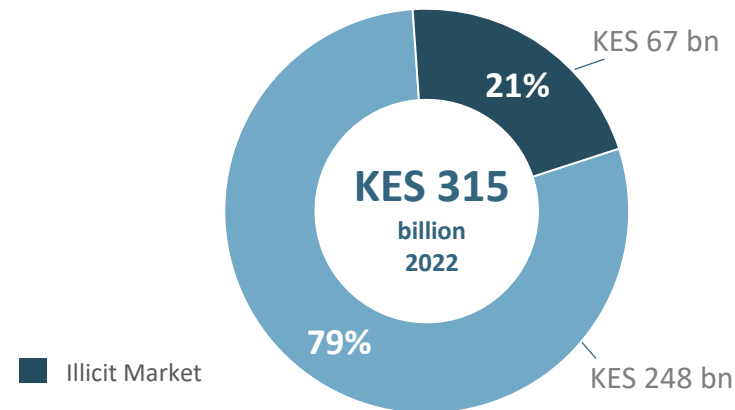
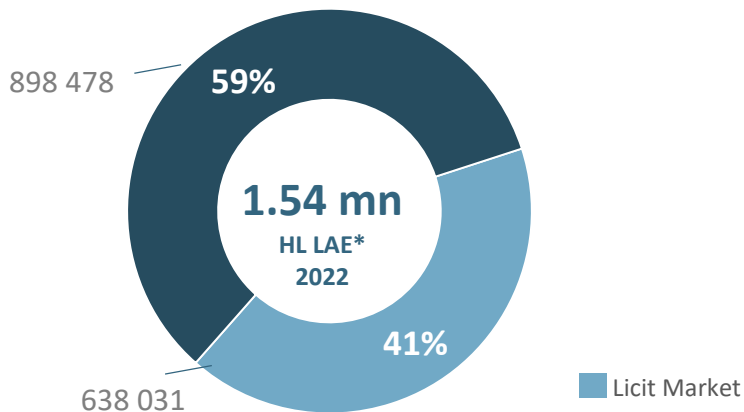
Illicit Category	Definition
Counterfeit and Illicit Brands	Fraudulent imitations of legitimate branded products, including refilling, falsification, and tampering. These beverages infringe the intellectual property rights of legitimate producers.
Contraband/Smuggling	Alcohol with original branding that has been illegally imported/smuggled into a jurisdiction and sold, evading tariffs/customs. Includes beverages brought across the border either in excess of the applicable traveller's allowance regulation or via so-called "ant smuggling".
Tax Leakage	Legally produced alcohol beverages on which the required excise tax was not paid in the jurisdiction of production.
Illicit Artisanal	Artisanal alcoholic beverages made for commercial purposes.

Executive Summary

Key learnings

- The **expansion of illicit alcohol** is gathering pace, both in volume and value, outstripping **licit volume growth** and increasingly encroaching into the higher-value spirit market.
- **Illicit artisanal** alcohol accounts for more than **half of the total volume** of illicit alcohol but the **real value** of illicit trade lies in **counterfeiting, smuggling** and rapidly developing **tax leakage**.
- **Fiscal loss** is primarily driven by mainstream and illicit manufacturers of distilled (spirits) alcohol attracted by its **high profitability**, efficient **production** and potential for easy sale into **licit channels**.
- **Mass-market, high-volume** brands are the main target of **counterfeiting and smuggling** but **smugglers** are also interested in **ethanol**, driven by increasing demand from **illicit commercial** alcohol manufacturers. A mix of **mid-market** and **premium spirit** brands are also targeted alongside high-quality **cider and beer**.

Despite a low value share of the overall alcohol market in 2022, growth in volume sales and consumption is significant



59% Illicit Alcohol Volume Share of Total Alcoholic Drinks 2022 (HL LAE)

- **Illicit alcohol volume** sales of **898,478** HL LAE now comprise **more than half** of all sales of alcohol in Kenya.
- **Licit** alcohol volume sales grew strongly across the period 2021-2022 by 63%.

21% Illicit Alcohol Value Share of Total Alcoholic Drinks 2022

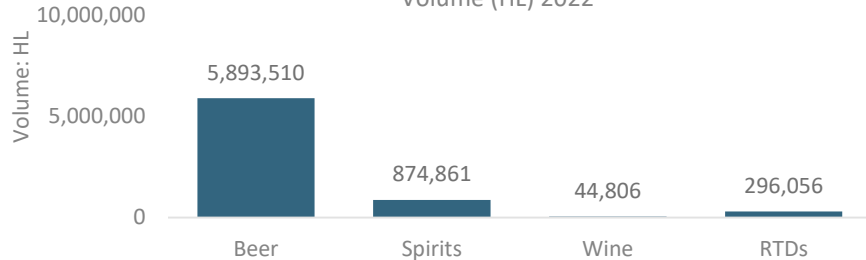
- **Value sales** of alcohol are dominated by **licit** alcohol at **KES 248.1 billion**. Values sales grew at 70% during 2022
- **Illicit** alcohol sales of **KES 67 billion** have seen strong growth in value since **2020**, reflecting its wider distribution and increased volume sales.

Spirits consumption continues to grow as variety in packaging sizes and affordability increases

Total Legal Alcoholic Drinks Volume by

Category

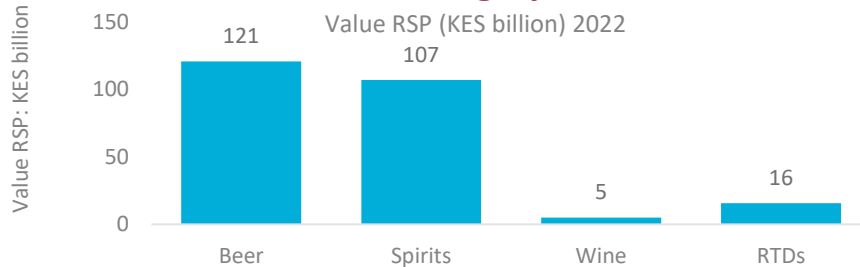
Volume (HL) 2022



Total Legal Alcoholic Drinks Value by

Category

Value RSP (KES billion) 2022



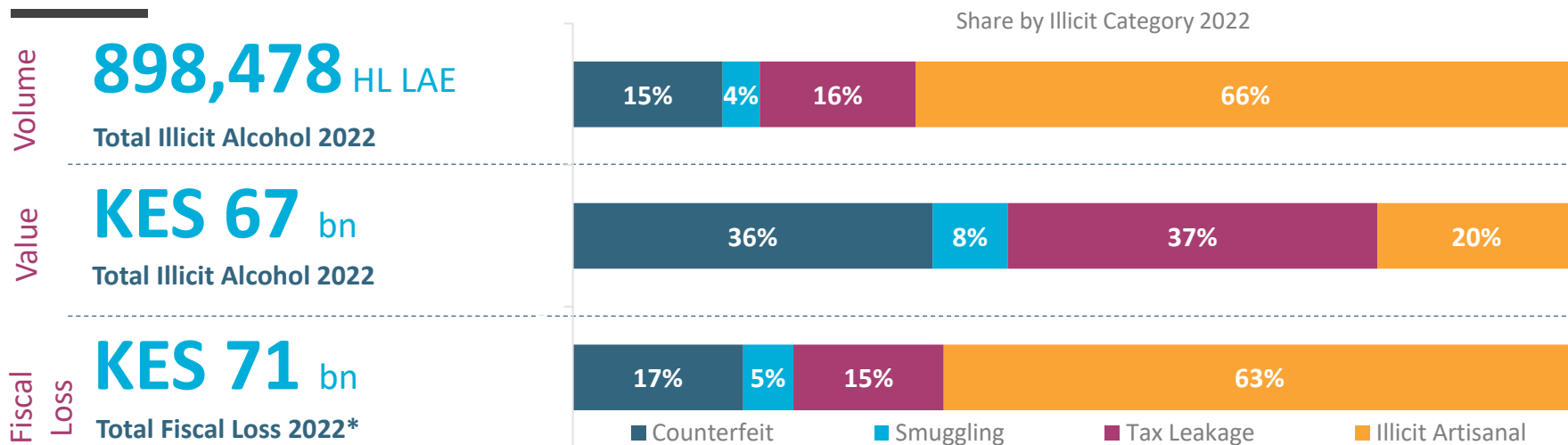
Beer is the largest category, but sales have been depressed by the **slow recovery** and reopening of **on-trade** outlets post-COVID-19 as well as a **consumer switch** to **lower-priced, higher-alcohol spirits**.

Spirits have widespread appeal in Kenya and are available at a **range of price points**

Gin is popular among **millennials** with **RTDs expanding** their presence through the appeal of **variety, affordability** and **suitability** for at-home and out-of-home drinking occasions.

Wine consumption is growing, particularly among Kenya's **wealthier middle class**

Illicit alcohol is widespread, readily accessible as illicit volumes continue to grow



- **Illicit trade in alcohol** is **widespread** in Kenya, affecting popular alcohol types such as spirits, beers and wines.
- **Counterfeit** and **smuggled spirits** are key categories of illicit trade but the volume of **illicitly artisanal spirits and home brew**, once present on a small scale in rural areas, is now widely available and produced on a commercial scale.

- The avoidance of payment of high taxes and duties is the driving force behind much of the illicit trade but especially of **tax leakage** through highly profitable sales of under- or non-declared production.
- Greatest **fiscal loss** is accrued through distilled (spirits) alcoholic drinks particularly in tax leakage and a growing trend towards premium spirit counterfeiting and smuggling.

Price differentials and profitability and encourage illicit trade and consumer purchasing



Affordability

Illicit alcoholic beverages are often **sold at a lower price** than legal drinks, as a result of noncompliance with tax and excise regulations.

Price differentials **driven by high taxes** and more **costly raw materials** for legal alcohol make cheaper, illicit alcohol beverages more affordable.

It also **encourages widespread consumption**, particularly among young people, many of whom are unemployed or poorly compensated for their work.



Accessibility

Illicit alcoholic beverages are distributed through **street vendors, taverns and drinking dens** as well as formal retailers including **licensed public events, liquor shops, grocery retailers, bars** and other hospitality outlets.

The illegal distribution network allows illicit alcohol to **infiltrate all channels** in the market, **undermining the integrity** of the alcohol industry.

Widespread **bribery and corruption** according to trade sources ensure the continued presence of illicit alcohol in all channels.



Enforcement

Minimal police focus during the pandemic coupled **with increased demand** has demonstrated the **profitability** of illicit alcohol to **traders** as well as **corrupt officials**.

Despite the existence of robust laws and regulations, **enforcement remains a challenge**.

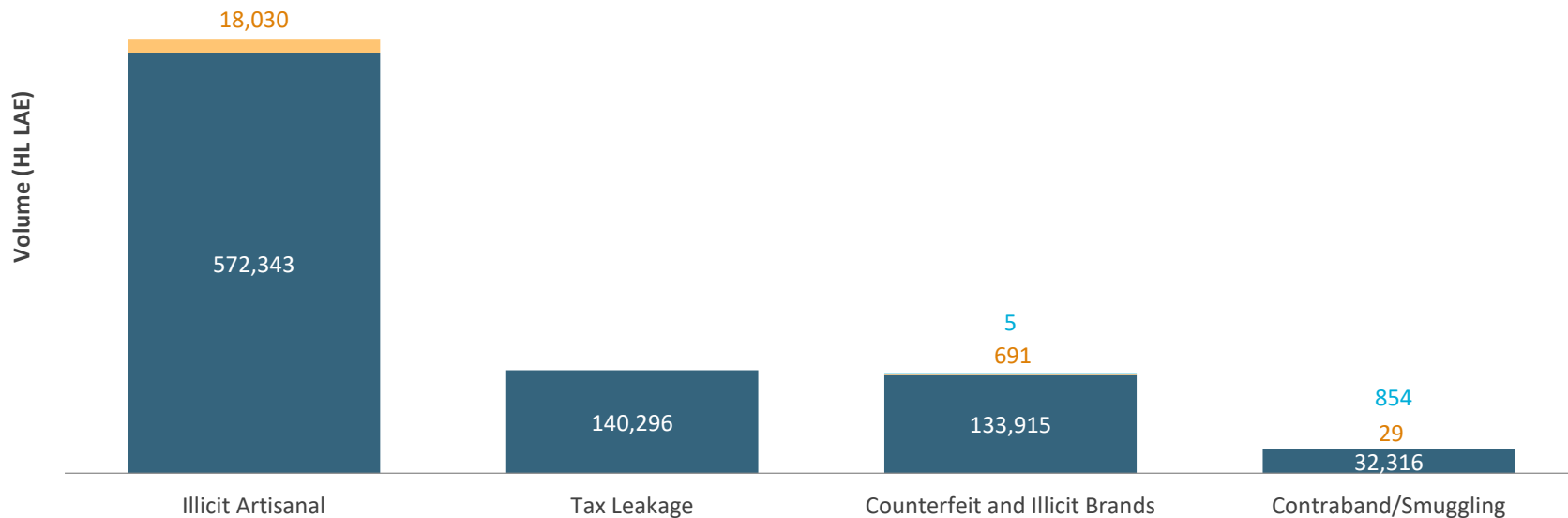
Authorities and the **court system** are slow to increase **enforcement, penalise or incarcerate** those involved in this trade, doing so usually in response to **fatal incidences**.

Current penalties and punishment is not seen as a deterrent

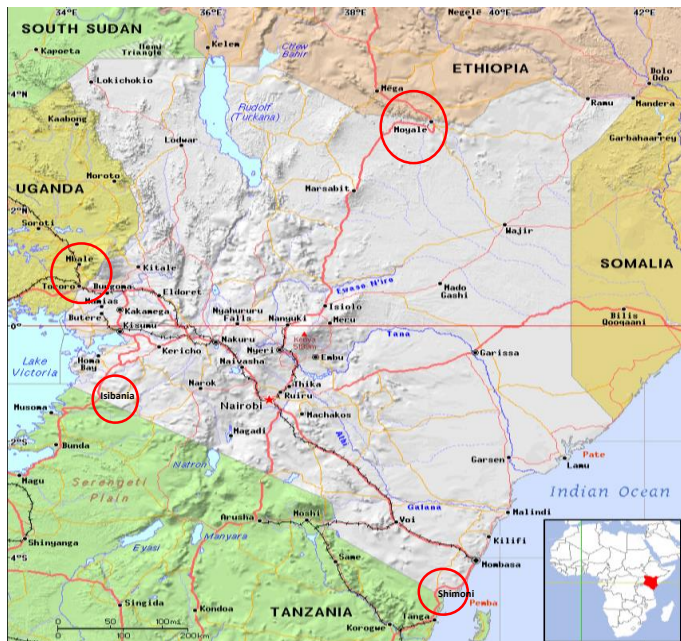
Spirits now dominate all forms and methods of illegality in the Kenyan alcohol market

Illicit Alcohol Market by Alcohol Type (HL LAE) 2022

■ Spirits ■ Beer ■ Other



Smuggled networks are well established transporting illicit ethanol to traders and wholesalers in Kenya



Map Source: www.mapsland.com

Production Cycle



There are multiple established routes for smuggling dependent on cargo type and size

- **Illicit ethanol traders** have resorted to **smuggling ethanol** into the country taking advantage of **rising local ethanol demand, price differences and higher ethanol availability** in Tanzania and Uganda.
- Smuggling of ethanol is also driven by **weak border patrols, widespread corruption and unmanned entry points** along Kenya's borders. **Isbania** and **Shimoni** (Kenya-Tanzania), **Mbale** and **Busia** (Kenya-Uganda) and **Moyale** (Kenya-Ethiopia) are popular routes.
- Smugglers may transport **200-litre drums of ethanol** across the border **disguised** and transported with drums containing **cereals or animal feed**.
- **Boda boda/motorbikes** transport **20-40-litre jerrycans** and distribute them to local, smaller-scale producers in towns and villages close to the border. **Panya routes** or **informal cross-border routes** are used in less patrolled regions
- **Cover cargo** that attracts **no or lower import duties** is used by truck drivers **smuggling ethanol** or other alcohol, paying **tax for the cover cargo** and thereby constructing a **legal and registered import record**.

A greater focus is being brought to illicit alcohol under the influence of new administration leaders

A coordinated multi-agency approach to eradication of illicit alcohol has been boosted by the direct support of President Ruto who has made its eradication a central plank in his administration. Led by the National Authority for the Campaign Against Alcohol and Drug Abuse (NACADA), joint initiatives have stepped up actions to combat counterfeiting, smuggling and illicit production through higher levels of investigation, border control, inspections, raids and closure of illicit distilleries. Concerted actions in the administrations of five counties in the Central Region involving all relevant state agencies are now seen as a potential model for future actions in other counties in Kenya.



Businesses, politicians, community leaders, police, customs and border control officials are on notice that **any involvement** with production, distribution or sale through licensed or unlicensed outlets will be considered **criminal activity** and be subject to punishment by the law.



The **East African Business Council** has advised member countries to **review contracts and costs** for digital tax stamp (DTS) system implementation. This advisory notice comes amid recent multi-million Swiss Francs **finances and penalties** imposed on SICPA, the Kenyan contractor, for **criminal activity** and **acceptance of bribes** by **Swiss courts in April 2023**. Action is needed in **Kenya** as **renewal of the DTS contract is imminent**.



Church and community leaders are also being encouraged to support **community initiatives** and **reporting of illicit activity** and operations in their areas as part of a **cohesive national approach** to stamping out illicit alcohol.



Centralise Control

Increase the powers assigned to the Kenyan Revenue Authority with a national campaign to formalise personal and business taxation.

Continue participation in enforcement by a central multi-agency focused on clearly defined KPIs based on levels of successful prosecutions.

Incentivise border controls and agents to ensure higher rates of enforcement.

Closer monitoring of access, distribution of ethanol (as a raw material) and packaging materials used.

Recommendations



Greater Premises Control

The combination of accessibility, and affordability as well as general economic pressures has contributed to the persistent demand for illicit alcohol.

Controlling easy access to illicit alcohol through licensed/unlicensed premises and sellers is critical to communicating intent to consumers.

Greater inspection, increased surveillance, traceability and monitoring of retail outlet inventory will make it more challenging for illicit alcohol producers to operate undetected.

Greater enforcement of illegal distribution of ethanol/packaging material across the value chain is required



Changing Perceptions

Increasing the potential of being caught alongside increased severity of penalties may change the assessment of the costs and risks associated with operating illicit breweries and distilleries.

For consumers, direct experience of the health damage from illicit alcohol is a main consideration, so highlighting trustworthiness of legal brands is key.

A clear message that the production and consumption of illicit brews is harmful and will not be tolerated is required to act as a deterrent and help reduce engagement in illicit alcohol production.

Q&A

Any Questions

Thank you

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