



Forget About Gas Price Hikes –

WHAT HAPPENED TO THE PRICE OF *TEQUILA*?

• *by Ian Foster*

Bar and restaurant owners throughout the world have been hammered by a huge increase in the cost of tequila over the past few months. In Southern California, the cost of a basic house-brand tequila has *more than doubled* – and it continues to rise with every passing month.

Because of the enormous popularity of the Margarita, North America's best selling cocktail, this has a significant negative impact on profits. For Mexican restaurant owner's, however, this is a major crises, often resulting in a ten percent drop in profits (ie: a pour cost change of 2 points or so).

"The cost of my house margarita has doubled," noted one Mexican restaurant owner in San Diego, "but I cannot double the price I charge. And house margaritas make up three-quarters of my liquor sales!"

In fact, the cost of the raw agave, which is used to make tequila, has risen almost tenfold in the past year.

WHY HAS THE COST OF TEQUILA SKYROCKETED?

The main reason is that consumers are buying a lot more tequila than they used to. Global consumption has doubled in the past four years, making tequila the fastest-growing liquor category in the world. And this huge demand for tequila, and especially premium tequilas, has risen much faster than the supply.

"[It's not a] severe shortage of agave that's driving up prices," notes Ramon Gonzalez, director of Mexico's tequila regulation board. "It's demand – and profiteering by distributors."

(Note: Southern Wine & Spirits refused to comment for this article).

The problem is intensified by the increasing popularity of all those premium tequilas made up of 100% agave. By international law, all tequila must contain at least 51% agave, while the other 49% can be made up of other spirits. Obviously, the 100% agave tequilas use up twice as much agave as the cheaper products. So for every customer who switches from cheap, mixed tequilas to premium tequilas, twice as much agave must be grown.

BUT WHY HAS THE COST OF THE CHEAPER TEQUILAS RISEN THE MOST?

That's because the big companies that supply tequila make more profit from the premium, 100% agave brands so they want to make sure that they use their limited agave supply for the high-end stuff. In fact, some producers have stopped making the cheaper mixed tequilas altogether. For example, Sauza has dropped their Giro brand of tequilas to concentrate on their booming line of premium tequilas such as Commemorativo, Hornitos and Tres Generacions.

Another reason is that in 1997 the World Trade Organization and the European Union adopted the Mexican government's position that only tequila made from at least 51% Weber blue agave grown in Jalisco state or five designated neighboring areas could be called tequila. Dozens of cheap brands produced in other Mexican states, the U.S. and Spain had to be relabeled, raising the tequila demand on Jalisco.

WHY DON'T THEY JUST PLANT MORE AGAVE?

While plantings are up 18-percent, the problem is that the agave plant grows very slowly. It takes ten years for the plant to mature enough to harvest. Way back in 1990, tequila makers did not forecast the tremendous

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Tequila costs!

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growth in tequila sales so they didn't rush out to plant a bunch more agave plants. Now it's too late and it may be five to ten years before enough agave plants have matured to ease the under-supply.

All through the 1990s, it has been a turbulent time for tequila growers. "In 1996, irate farmers organized to protest against their exploitation by some tequila producers. Their subsequent blockade cost the industry millions of dollars. The standoff only ended when producers agreed to increase the price of agave piñas by 30% - to 850 pesos a ton, or about \$8.50 US. This price was still lower than the 1,000 pesos a ton received for piñas in the late 1980s.

In mid-1997, the tequila industry was shocked when producer Don Jesus Lopez Roman was shot in front of his factory in a gangland-style execution. Roman - whose distillery Tequila San Matias was founded in 1884 - had been a leading advocate of the move to higher standards in the industry and allegedly unpopular for his very vocal comments. He wanted all tequilas to be bottled in Mexico, banning bulk exports to ensure quality and content"

(From www.tequilafancy.com).

IS THERE A PROBLEM WITH TEQUILA QUALITY?

The Mexican government's biggest concern is that the increased demand will result in more tequila rip-off artists. They have clamped down hard on producers who use less than the required amount of agave in their tequilas. In 1998 several Mexican distilleries were closed down and 67 brands were suspended for diluting the amount of agave.

Perhaps a bigger problem is what happens after the tequila is exported. About 85% of export tequila is sold in bulk and bottled outside of Mexico. Some unscrupulous bottlers have been caught adding sugar, which raises the alcohol content, so that they can cut down on the amount of tequila. And recently, some American producers have been making pre-mixed "margaritas" that don't even contain any tequila. Instead of tequila, they use flavored grapes or malt. They exploit a loophole in the law by labeling it as a "pre-mixed margarita" instead of "tequila."

Some producers are so concerned that they have asked the government to change the legal definition of tequila so that every tequila must be made of 100% Mexican agave - which would

effectively eliminate the bottling of exported bulk tequila in other countries.

Herradura has been a vocal opponent of bulk exports, arguing that mixed tequilas and adulterated exports damage the image of tequila and Mexico. In fact, Herradura refused to be bought-out by Seagrams in the early 1990's because Seagrams wanted to produce mixed tequilas.

HOW CAN I RESPOND TO THE PROFIT SQUEEZE?

For the most part, there is not much that can be done to bring your costs in line. The costs for all house tequilas have risen dramatically. Some restaurant chains have looked at buying South African tequila-knock-offs. These spirits are made from South African agave plants but legally they are not tequila. Waiting until the price decreases is not an option - if anything the costs are expected to keep rising.

Many restaurants have eliminated their house tequila and switched to a premium well. The rationale is that since the cost difference between the cheap tequilas and the better brands has narrowed so much, they might as well give their customers better tequila.

In reality, the only solution is to raise your margarita prices.

Unfortunately, even though the cost has doubled, there is really no way to double your prices. Most restaurateurs will have to be content simply to cover their increased costs. For example, prior to the dramatic cost increases, a 1-¼ ounce shot of tequila cost around 26¢ (based on prices in Southern California). Today that same shot of tequila will cost around 54¢. Thus, just to cover the increased cost, you will need to raise your Marg and tequila prices by 30¢ across the board.

Of course, that doesn't include any reasonable amount for profit. Perhaps a more realistic response would be to raise prices by 75¢ to \$1.00.

In the next issue of The Booz Nooz, we'll try to find out why your distributors have been quietly increasing your costs on a whole range of other products - from Absolut Vodka to Jack Daniels.



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