

Padua 2017 Abstract Submission

I want to submit an abstract for:

Conference Presentation

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Keywords

counterfeit wine, food safety china, intellectual property China, Chinese wine

Research Question

How do Chinese wineries overcome barriers to credibility resulting from incomplete enforcement of quality standards (food safety, intellectual property, and product authenticity)?

Methods

Qualitative fieldwork included unstructured/semi-structured interviews, repeat visits, participant observation for 4-6 weeks each year (2013-2016). 8 producing regions, 50 wineries, plus distributors, government officials, educators, media, farmers.

Results

1. Technological innovation: minimize transactions through authenticated online marketplaces (TMall) and direct-to-consumer sales (Wechat);
2. Contracting up with trusted multinationals
3. Personalized public relations campaigns

Abstract

Firm innovation in the absence of effective regulation: Overcoming barriers to credibility in Chinese wine

1. Introduction / Short Abstract

Chinese firms often struggle to overcome the reputational effects of inadequate regulation and law enforcement, particularly in the areas of food safety and intellectual property. Wineries bear the brunt of quality scandals, not only because China is an as-yet-untrusted emerging wine region, but because wine is both a luxury good (subject to counterfeit trade) and an agricultural product (subject to food safety standards). Research on the development of effective regulation in China tends to focus on reasons for inadequate enforcement and avenues for institutional change in particular sectors, such as food safety (Jia and Jukes 2013; Kerns 2016) or the importance of informality/guanxi in the wider economy (Z. Yang and Wang 2011; Puffer, McCarthy, and Boisot 2010; Allen, Qian, and Qian 2005). Related research in economics seeks to quantify the effects of improved regulation (Awokuse and Yin 2010; Candelin-Palmqvist, Sandberg, and Mylly 2012; Lin, Lin, and Song 2010). By contrast, the strategies of successful firms in overcoming regulatory constraints have received far less attention, and the wine industry remains virtually ignored. We address this gap by looking at the portfolio of strategies that enable Chinese wineries to signal quality in an environment of low consumer trust. Data are based on extended multi-method fieldwork (4-6 weeks each year, from 2013-2016) with 50 wineries in 8 Chinese wine regions. We find that successful wineries employ a proactive, three-pronged approach: 1) technological innovation to minimize

transactions through authenticated online marketplaces (TMall) and direct-to-consumer sales (Wechat); 2) “contracting up,” working with trusted multinational distributors or suppliers; and 3) personalized public relations campaigns, including personal stories, wine tourism, and targeted media relationships.

2. How bad is bad? Regulatory constraints, scandal, and reputation management

Consumer confidence has long been an uphill battle for Chinese wineries. Ubiquitous experiences with faulty wine at the supermarket are compounded by old, but memorable tasting notes that evoke “urinal crust” (Veseth 2008). But in China, even premium wine is suspect. Wine enthusiasts are concerned about counterfeit labels or bulk wine poured into premium foreign bottles (Muhammad et al. 2014). Although counterfeit wine is a global phenomenon, much of the technological innovation to fight it has been implemented in response to the limits of Chinese intellectual property law (Bao 2010; Kehoe 2013). As media reports multiply, middle class wine connoisseurs are primed to doubt both the quality and the authenticity of wine in China, knowing that they risk overpaying for inferior wine and the wounded pride facing victims of fraud.

In terms of food safety though, alcohol represents far less risk than primary agricultural commodities, so most buyers are concerned with signals of authenticity, with some exceptions. Cathay Pacific was happy to feature a 2008 Grace Vineyard as the first Chinese wine on a major international airline, except for one serious concern. In the same year, international outcry followed a Chinese powdered milk scandal that had killed infants and poisoned hundreds. Of course, there is very little overlap between the dairy and wine industries, but the concern was not unfounded. Chinese and foreign consumers would be increasingly skeptical as more and more public scandals challenged the ability of Chinese regulators to enforce standards. When a report charged Changyu wine group with exceedingly high pesticide residues, its stock plummeted overnight (“Gov’t Researcher Responds to Chinese Wine Contamination Allegations” 2012). This prompted a government-supported media blitz that is a case study in corporate crisis management. The stocks rebounded, but consumers openly mocked the general manager’s “preposterous claim that only if one drank 123 bottles of its wine on a single day would it be harmful to health” (G. Yang 2013, 15).

3. Technological innovation: minimize transactions through online marketplaces

Direct to consumer sales promote consumer trust by minimizing the role of intermediaries who might sell fraudulent products. For many Chinese consumers, online retail is the most trusted form of shopping, having helped to make Alibaba (the umbrella corporation for Taobao and TMall) the largest retailer in the world (Goenka 2016). The infrastructure for online shopping and affordable shipping in China is among the most efficient in the world, including for micro-enterprises, whose entire inventory is liquidated by word of mouth, but still conduct most transactions on Wechat. Of course, the level of security is increasing in the scale of the firm, so online marketplaces offer different levels of protection. Alibaba has been sued more than once for participating in the trade of counterfeit luxury products (Raymond 2015), but it has developed sophisticated strata for price discrimination. Each subsidiary provides an online marketplace with distinct standards for monitoring as well as different avenues for redress in the event of complaint.

Elite wineries create authenticated storefronts on TMall, so that their products can only be purchased from them. Significant barriers to entry (registration and annual deposits of thousands of dollars) deter most would-be scammers, but there are other security measures in place. TMall stores must be formal companies with physical stores and companies abide by a multi-tiered insurance and consumer protection system. Most firms sell on the larger, less secure platform, Taobao, which has intellectual property protection measures in place, but they are far less technologically sophisticated and far less trustworthy. Monitoring is increasingly accomplished through co-regulation (Sui 2015). This includes public sector cooperation and regulatory innovation, despite inconsistent enforcement in court (Ferrante 2015), complemented by technological innovation in the form of firm-level contract enforcement as well as cyber-security.

4. Contract up: Partnerships with trusted multi-national distributors and suppliers

In the absence of consumer trust, elite producers align themselves with the most obvious sources of perceived legitimacy, multinational conglomerates whose reputations are established. Distributors like Torres, Summergate, and East Meets West are primarily importers of foreign wines, so they benefit from credibility, but they have reputations to protect. Each distributor sells a restricted selection of very few Chinese wines and only one or two

wineries. Representatives invest in long-term relationships with their wineries, including personal inspections and tastings, only to sell a relatively small quantity in a restricted set of bars and restaurants. For the most part, distributors find that demand for Chinese wine comes from curious foreigners. Meanwhile, the wineries sell the bulk of their inventories independently, online and to Chinese consumers. To some extent, each partner is investing in future potential, but much of the immediate benefit of a distributor is reputational, in the signaling of quality, transparency, and credibility.

The same quality signal can be identified in supplier contracts for corks, barrels, and other equipment. The vast majority of supplies are imported, with the most successful wineries working with exclusive partners.

5. Personalized public relations campaigns

The personal story is a critical component of wine branding around the world, particularly for small producers who struggle with product differentiation. The relevance of personal ties is compounded in an environment of inadequate regulation and consumer trust, as is evident throughout the literature on institutions and growth (Zysman 1994; Haggard 2004; Chen, Chen, and Huang 2013). Branding and consumer trust in Chinese wines involves extensive investment in actual personal ties, but also in the image of a personal connection to the winery. Critically acclaimed wineries tend to have one person representing the public face of the winery, accessible to consumers and regularly appearing in the media. Surprisingly to many, several of the most celebrated Chinese wineries are owned and run by women, who are in charge of daily operations and public relations. For each of these, much of the initial investment involved fathers with important industry and government connections, but who are now relatively invisible.

As the number of wineries multiplies, investment in wine tourism has expanded, with small guest houses and opportunities to tour most wineries. These investments serve a variety of purposes, but most customers will never visit a winery. The expanded offerings serve to signal transparency and business acumen, promoting consumer trust. By promoting consumers' ability to visualize wine production from the grower to the consumer, wineries signal the credibility that regulators are unable to ensure.

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