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Title
From Stalinist Economy to a small business economy:
Wine business in transition – the example of Georgia

I want to submit an abstract for:
Conference Presentation

Corresponding Author
Lars Vigerland

E-Mail
lars.vigerland@sh.se

Affiliation
Södertörn University

Co-Author/s

Name	E-Mail	Affiliation
Erik Borg	erik.borg@sh.se	Södertörn University
Paulina Rytkönen	paulina.rytkonen@sh.se	Södertörn University

Keywords
SME, Georgia, Transition economy, Market economy, Ownership, Strategies, Family business, Initial Public Offering, IPO, Governance

Research Question
What strategies and conditions small and medium sized enterprises undergo in a transition from a former Soviet planned economy to a more liberalized economy aiming for an international market?

Methods
Secondary data available at company home pages of the entire population of Georgian wine producers listed by the Georgian ministry of agriculture and Georgian Wine Association used in regression analysis and possibly also multiple correspondence analysis (MCA).

Results
The aim is to contribute with new knowledge about the process when small or medium sized enterprises (SME) undergo transformation from a Planned economy to a Market economy.

Abstract
The wine industry in Georgia is rapidly transforming from an artisan activity conducted by families for domestic consumption and firms producing bulk wines for a low-cost segment of the Russian market, into a global player with modern businesses that strongly lean on a millenary heritage to market their products. Previous research about the Georgian wine market is scarce and focused mainly on describing the overall changes in the business in terms of more general and rather descriptive aggregate production development and understanding some of the overall strategies adopted by the industry (Cramon-Taubadel & Saha, 2015; Georgian Wine Association and Georgian Incoming Tour Operators Association, 2012; Kharaishvili, et al., 2014; Mikava, et al., 2017; Sakvarelidze,

2017; Wolfe, et al., 2013, and many more). However, a more analytical view of how the modernization process has taken or is taking place is still lacking.

After a brief period as a sovereign country after the Russian Revolution, Georgia was forced into the Soviet Union as the Georgian Socialist Soviet Republic. Thus, for most of the 20th century, the command economy of a Soviet model in Georgia prevailed. Freedom from the Soviet Union occurred in April 1991, this period usually referred to as glasnost. From this year, the Georgian economy has been slowly striving towards a traditional market economy and this is usually referred to as a transition economy (Areshidze, 2007; Jones, 2013). The Freedom House Institute designates Georgia as partially free (https://freedomhouse.org/report/freedom-world/2018/georgia, retrieved on January 31, 2019). Apart from changes of macro-structures and economic conditions within former Soviet republics (e.g. Manning & Uplisashvili, 2007; Radas & Bozic, 2009; Rehn & Taalas, 2004), other countries throughout the world have also gone through market transition with its challenges such as China (Anderson et al., 2003; Chow Kong Wing & Fung Ka Yiu, 1996; Tan & Veliyath, 2009). Georgia is likely to face similar problems as other transition economies as well as many for Georgia and for the wine industry specific challenges.

The aim is to contribute with new knowledge about the process when small or medium sized enterprises (SME) are undergoing transformation from a Stalinist economy to a free market economy, such as the wine industry in the former Soviet republic of Georgia. The perspective is the level of an enterprise, i.e. a micro perspective. The contributions made by this article is that the enterprise level perspective can help us to understand what strategies and conditions small and medium sized enterprises undergo in a transition from a former Soviet planned economy to a more liberalized economy and also to understand the wine industry in Georgia that has either been focused on the production on low cost and relatively low quality bulk wines aimed for the Russian market, or a domestic production aimed only for the inner family circle, to a more international market competing with traditional wine making regions in countries such as France, Italy, Spain and the US. In many cases the change of production from quantity to quality is very challenging as it is hard to meet consumer demands of more nuanced preferences. It is also hard to enter an existing market with extreme competitiveness with a product until now from a relatively unknown region with new attributes such as the concept of natural wine (qvevri) and new sorts of grapes. Wine consumption is also closely linked to images of cultural contexts and attributes relatively hard to change. “New world” wines were eventually successfully introduced on the international wine market some decades ago; the Georgian wine industry faces most likely similar challenges.

The main questions to be answered are: Which are the main drivers behind business owners’ decision and strategies about the future of their firms? When do wine makers take the step transforming a home activity for self-consumption and make the enterprise into a business or take the step transforming production from quantity to quality? Why do some businesses remain family-owned and family controlled? When new partners or co-workers from out of the enterprise are invited to join, do they have a competence in the production from the traditional wine industry, do they have marketing knowledge from the traditional wine industry, do they contribute with capital or is there any other strategic reason for inviting new partners or co-workers? When are the enterprises – to a varying degree – made joint stock companies or even prepared to go public? What specific problems are there in Georgia and in the Georgian wine industry compared to the macro-structures and economic conditions of other regions such as other transition economies as well as traditional market economies, especially the wine industry of other regions?

The wine markets
The Georgian wine industry has different types of businesses, ranging from large and internationally oriented companies to very small family businesses. The common issue to them, however, is the challenge of marketing and selling a relatively sensitive product such as wine (Beverland, 2005) from a country that is not only relatively unknown to the wider public outside the Southern Caucasus and the former Soviet Union, but also an unknown region for wine production. Other traditionally wine-producing regions have been forced to change (e.g., Rossi, 2012), but the Georgian wine industry has been forced to undergo radical changes through the conflict between Russia and Georgia, which spilled over into the trade relations. Georgian wine has occasionally been banned in Russia, which was the dominant market before 2006, forcing the wine business to carry out a market reorientation (Anderson, 2013).

Family Business and Initial Public Offering

There are also other considerations than marketing and sales within a family-related business. To keep the business closely linked to the family or to a few personally involved owners are ways of ensuring that good quality and good finances are maintained (Broccardo et al., 2015). One of the challenges of business activities is to choose goals and strategies as well as ways of financing the business. A strategy of expansion or of owner change can be done through initial public offerings (IPO). Such a strategy is common and feasible in family firms (FF) in traditional market economies (Mahérault, 2000; Mazzola & Marchisio, 2002), but the Georgian economy is still struggling with matters that are fully accepted and functioning in other economies. As an example of the fact that the Georgian economy has not yet reached maturity is that the only marketplace for trading financial instruments is the Georgian stock exchange (GSE) established by USAID and which does not yet list more than 33 companies (GSE, https://gse.ge/en/about-gse, 2019).

Corporate Governance
It is often argued that family control in family firms (FF) is a way to reduce the monitoring costs and the free-rider problem (Andersson & Reeb, 2003; Schulze et al., 2001; Tufano, 1996). Trust should be an important aspect to consider in an economy with limited experience of the functioning of a market economy such as the Georgian market. The time horizon and objectives may differ between family firms and non-family firms. Family firms have a tendency of longer time horizons and are more focused on wealth maximization (Chami, 1999; James, 1999). On the other hand, there are studies that show that family firms are financially ineffective and instead create agency costs (Anderson et al., 2003; Anderson & Reeb, 2003; Morck & Yeung, 2003).

The Pecking Order Theory
A matter close in relation to both IPO and Corporate Governance is choice of financial structure within a business. The Pecking Order Theory (Myers, 1984; Myers & Majluf, 1984) claims that companies choose financial structure according to a hierarchical principle: primarily a business use internal financial resources such as accumulated profits, company equity, owner capital and even unpaid work, secondary loans, both bank loans and public corporate loans, and tertiary capital transactions from external parties, thus offering different types of ownership or part ownership. In this way, companies choose a capital structure with a gradually larger information gap between management, creditors and investors, and thus also creating an increasing uncertainty (Myers, 1993; Myers, 2001).