

## Quality and Value Creation on the Premium Wine Market

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### Summary

- Research questions:** How does the value creating process on the wine market work? How is quality perceived and measured? And, are the wineries themselves able to influence the quality perception of their product on the market?
- Methods:** Empirical study across different premium wine producers in Australia and California using a standardized questionnaire.
- Results:** There is a significant interdependency between quality, price, and reputation. Institutions, like wine experts, wineshows, and wine producers influence the quality perception on the market actively and reduce uncertainty and, thereby, create the basis for market transactions.
- Structure of the article:** 1. Introduction; 2. Literature Review; 3. Research Question & Method; 4. Results; 5. Conclusion; 6. About the author; 7. References.

### 1. INTRODUCTION

Wine is an intriguing and complex product with distinctive qualities that make it significantly different from other standardized, typically manufactured, goods. The market for wine is highly diversified and differentiated. The objective of this study is to examine institutions and mechanisms that influence reputation and the value creation on the premium Australian and Californian wine market and, furthermore, how winemakers influence quality perception actively and reduce by that uncertainty on the market.

Quality is described by intrinsic and extrinsic quality dimensions and consists of objective, relative, and subjective quality factors, which determine the value creating process in the Australian and American wine industry.

The social economic model developed in this study understands the wine market as an environment where rationality is socially constructed by institutions, producers, and consumers. Necessary specific criteria are generated by the market itself helping the stakeholders to make decisions under conditions of uncertainty. Therefore, the motivation and behavior of winemakers and winery owners is reviewed to understand, how they approach quality, reduce uncertainty, and influence the quality perception of their product by establishing business models closely related to their individual resources (e.g. tradition of the vineyard, reputation of the region, size of the winery). Interviews with winemakers represent regional differences and give prove to the bundle of quality influencing and differentiating factors from which the wineries create their specific quality comprehension.

Interdependency of quality, reputation, and price is analyzed to establish the theoretical framework for the survey. This includes the challenge to define and conceptualize the quality term on the wine market and to face the complexity to finally be able to describe the producers' view on quality. Along with the concepts of price and reputation, quality indicators and correlates are presented, which are checked empirically.

After that the focus is on experts and other institutions rating quality on the wine market and reducing uncertainty and, thereby, influencing market behavior.

The interview survey represents the second chapter of this article. It examines the business model and strategy of the selected wineries, the winery's quality approach and understanding, as well as the resources of the winery to test the following hypotheses:

1. Institutions and mechanisms of reputation are the value creating factors on the wine market. Quality is, by that, socially constructed.
2. Wineries influence, with regard to their resources, this quality creation process actively and independently.
3. The wineries are able to influence the value creating factors significantly by active profiling.

#### *The New World*

Globalization of the wine industry is increasing as global wine exports as share of global production have increased from 15% to 25% over the Nineteen-Nineties (Hussain et.al., 2008, p. 33), while the total wine production and consumption have been decreasing faintly over the past two decades (Anderson, 2003, p. 659). As globalization is not new for the wine industry when regional wine producing and consuming countries have been trading for more than thousand years, the bulk consumption and production was relatively localized until the early Nineteen-Nineties. Thereby, wine productions in far-away countries were isolated from each other. These traditional consumption patterns changed in recent years (Hussain et.al., 2008).

Today the geography of the world's wine industry is generally differentiated in *Old World* and *New World* countries. Even though the fact that this simple dichotomy was recently criticized for

ignoring the significant and rapidly expanding production and consumption of wine in developing countries as India and China (Banks, 2009, p.57), it remains sufficient for the basis of this study, which focuses on two classical New World wine producing countries: Australia and the United States of America. While the Old World countries, defined as those within Europe, have a long and uninterrupted history of wine production, the New World countries, defined as those outside Europe, have a winemaking tradition that is only a few generations old (Hussain et.al., 2008).

America's global reputation for fine wine is relatively recent. The often mentioned key event was the success in a blind-tasting in Paris in 1976, when several American Cabernet Sauvignon wines beat some wines from Bordeaux (Lukacs, 2000). After that the United States became an important wine producing and consuming country. Today, the United States are the biggest wine consumer (based on total volume) and the fourth biggest producer of wine (Hoffmann, 2006). However, due to diverse consumer behavior patterns, the United States still have a relatively low per-capita consumption of wine. Only 10% of the adults make 90% of all wine purchases. Thereby, the future potential of the domestic market is enormous by converting more Americans to wine from other spirits.

While over two-thousand wineries exist in the United States, the five biggest wineries produce two-thirds of the domestic wine market. Additionally to the large wineries, diversified conglomerates and wine groups represent a large part of the wine production and, are thereby able to enjoy both economies of scale and scope (Hussain et.al., 2008, p. 36). This is similar in Australia, where four companies are responsible for 80% of the production.

Australia is the seventh largest wine producing country today and the most threatening competitor to the United States domestically and in their export markets. Even though Australia produced only 1% of the wine worldwide in 1970, the production grew over 500% in the following thirty years. With relatively small per-capita consumption rate of 22 liters per year - similar to the United States - Australia was and still is highly motivated to succeed mostly in the export markets (Hussain et.al., 2008).

As described before, the American and the Australian wine industry have had a similar history and development until today. Both countries developed powerfully over the last four decades and are mostly represented by a few large wine producing companies, which are responsible for the bulk wines on the domestic as well as on the export markets. These wines are mostly industrial produced mass wines in the *non-premium* or *commercial premium* segment of the market. But there are also independent, small, and boutique-sized wineries in California as in Australia, which produce *super-plus premium* wines (Anderson, 2003).

With the entire wine industry booming, the premium segment was growing as well. Additionally, in each of the markets a substitution of quality for quantity could be observed. While premium bottled wine sales have been growing steadily over the last ten to fifteen years, non-premium (cask) sales have been declining (Anderson, 2003). These premium companies and their business models are in the focus of this study. The quality oriented business model of the boutique-sized to medium-sized wineries is separated from the mostly quantity oriented approach of the industrial wineries (Scott Morton et al., 2002).

## 2. LITERATURE REVIEW

The alleged easiest questions can sometimes be the hardest to answer. Even though the quality term is one of the most frequently used in winemaking, wine marketing, and generally wine describing, it remains one of the greatest challenges to determine what exactly makes a wine good and what wine quality really means.

### *The Quality Approach*

Personal taste, absence of faults, complexity, balance, length, personality, ageability, intensity of bouquet and flavor and varietal correctness are some of the most regular elements describing wine quality in literature (Basset, 2000), but product quality is considered to be difficult to understand (Garvin, 1984; Zeithaml, 1988).

Several studies have examined wine quality and worked on components of wine quality (e.g. Jover et.al., 2004, Botonaki, et.al., 2004). These studies focus mostly on quality in connection with purchasing or deal with legal quality frameworks which consider the origin of the wine as the most important quality indicator (Charters et.al., 2007). The subjectivity and the *quasi-aesthetic character* make it particularly difficult to define wine quality satisfactory (Charters et.al., 2005).

This study examines the quality from the producers' perspective and, thereby, links the quality as close to the wine itself as possible. The objective is to operationalize the quality term to find the indicators which define quality in wine.

Due to the fact that it is hard to define quality accurately, most of the studies so far looked at a perceived rather than an actual quality (Charters, et.al., 2007). Wine is an experience good and quality perception contains as a result a strong subjective share (Zeithaml, 1988), but there are objective aspects as well.

Jover et.al. set up seven dimensions of wine quality: (1) origin; (2) bouquet, flavor and balance of the drink; (3) vintage; (4) ageability; (5) image; (6) presentation; and the (7) acuteness, which is the aromatic complexity and intensity of the bouquet (Jover et.al., 2004, p. 457f.). In that way only two of the seven dimensions are intrinsic to wine, while the others are extrinsic characteristics. Thereby, Jover et.al. underline an important issue about wine quality. He points out that the "extrinsic quality cues are related with expected quality, while intrinsic quality cues are related both with expected quality and experienced quality" (Jover et.al., 2004, p.464). Whereas only bouquet, flavor, and balance as well as acuteness are directly connected with the experience of the wine, other factors are quality indicators as they are a sign of the expected quality. Whether these (or other possible) quality indicators are supposed to play an important role in winemaking and business strategy of wineries, will be part of the empirical analysis.



Figure 1: The Dimensions of Wine Quality (cf. Charters et.al., 2007, p. 1005)

### *The Quality Concept*

A recent study examining wine drinkers' perceptions of wine quality showed how wine drinkers can be grouped based on the specific quality dimensions they focus on. Furthermore, the study presents quality as a multi-dimensional construct and that consumers connect with wine depending on their individual involvement levels (Figure 1; Charters et.al., 2007, p. 997).

From the wine drinkers' perspective wine quality has distinct components, which could be split up into two types; external quality dimensions and, secondly, the experiences during consumption. The model which resulted from the analysis leads to a further differentiation of the dimensions of wine quality.

As described before, the main differentiation is between Intrinsic and Extrinsic dimensions (Olson et.al., 1972; Charters et.al., 2007).

To start with the extrinsic dimensions of quality, which are factual and measurable or at least observable, but not detectable by the consumer at the moment when drinking the wine. In Charters' and Pettigrew's study the consumers mentioned the quality of the raw materials and the winemaking process as crucial. They looked for consistency of wine from bottle to bottle, absence of faults and drinkability.

Furthermore, the marketing aspects were included as factors for quality. Some consumers looked for a nice label and directly linked that to the reputation and the price of the wine. By this it became obvious that symbolic motivation plays a role in the concept of quality (Charters et.al., 2007, p.1001).

The intrinsic quality dimensions were recognized to be of more importance than the extrinsic dimensions and were a larger category, too. Pleasure and enjoyment of the wine resulted as the main quality dimension. Almost every informant

talked about that issue. Additionally appearance and the gustatory dimensions, with balance, taste, drinkability, smoothness, mouthfeel, body, concentration, and complexity, were pointed out (Charters et.al., 2007, p.1001ff.).

Finally, paradigmatic dimensions and the potential of the wine to age were considered by the informants in the study. It was of importance whether the wine was able to reflect his origin and varietal purity (Charters et.al., 2007, p.1004). Overall, Charters and Pettigrew showed that wine-drinkers perceive quality multi-dimensional and that interrelation of different factors was complex, with extrinsic and intrinsic dimensions. The intrinsic dimensions seem to be the most significant for the consumer at the point of drinking (Charters et.al., 2007, p.1004). Interestingly extrinsic dimensions like production methods, faultlessness, and the grapes were stated to be catalytic or indicating quality - even if their precise influence may not be fully understood. Furthermore, they showed that the varying involvement levels of the consumers influence the individual quality perception of each consumer (Charters et.al., 2007).

### *Quality Framework*

The complexity of the quality term led to the examination of factors which correlate with quality (Garvin, 1984). This includes either antecedents to or the results of product evaluation (Charters et.al., 2006, p. 468).

In order to create structure out of the chaos of quality factors, the following framework categorizes quality into four areas. The composition defines quality by two related but distinct dichotomies as presented in Figure 2. This figure shows that each concept of quality can exist independently and in different combinations:

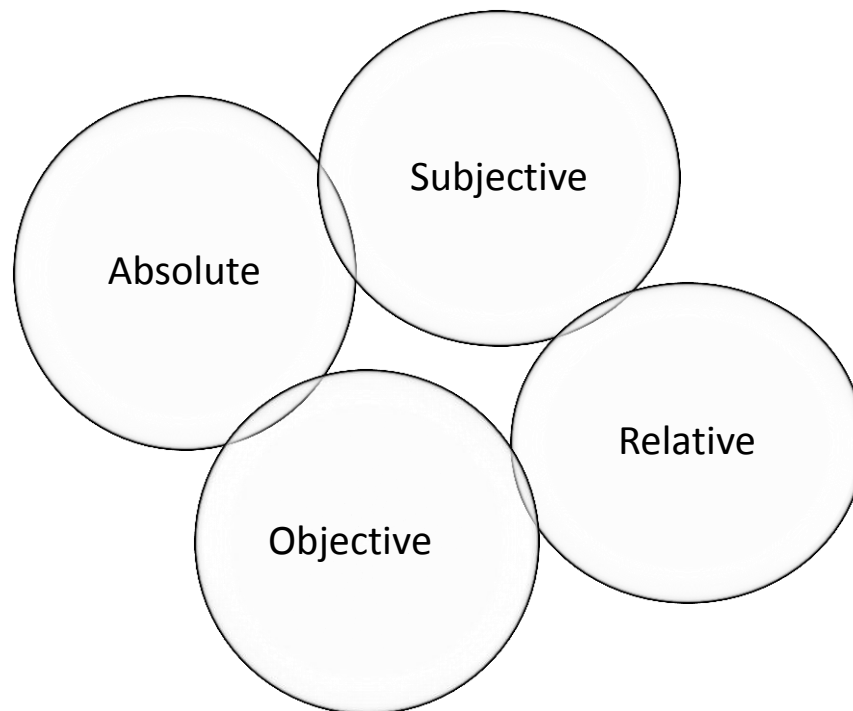


Figure 2: Framework for Quality (cf. Charters et.al., 2006, p. 470)

*Objective quality* is observable and can be measured by external criteria, while *subjective quality* only exists as a personal experience. Furthermore, *subjective quality* relates to individual emotions and taste; e.g. attractiveness. *Absolute quality* is fixed, independent of other variables and timeless, as *relative quality* exists only in relationship to other factors, e.g. price or personal taste (Charters et.al., 2006 p.469).

#### *Reputation – Expected Quality*

“When the true quality of a product is not known before purchase, consumers may rely on a firm’s reputation to form expectations of the product’s quality” (Landon, 1998, p. 628). Under these conditions prices will strongly depend on the company’s reputation (Klein et.al., 1981). This underlines the interdependency of the three concepts of price, reputation and quality. Several theoretical approaches exist which describe the effects of reputation on price as on quality, but only few empirical studies examine the factual effects. Landon and Smith examined the impact on price of current product quality and reputation using data from the market for Bordeaux wine. They developed a model in which price is a function of current quality and expected quality. Furthermore, they concluded that reputation – which they

understood synonymous to *expected quality* – and current quality significantly influence the price of a wine.

Additionally, they found out, that the influence of reputation is in fact twenty times greater than the influence of the current quality on the price (Landon et.al., 1998).

The results of Landon and Smith are especially applicable to experience goods and to markets where consumer information on product quality is incomplete and/ or elusive; like the wine market. Therefore a strong reputation is not only a competitive advantage, but also legitimation to establish high prices on products. It takes time to set up a reputation for high quality that would yield a significant price premium. Still, they found evidence that consumers consider long-term reputation to be a better indicator for current quality than more up to date quality actions. Moreover, the government- and industry-determined collective reputation indicators, like the appellations and classifications in Bordeaux, seem to have a weak direct impact on the price, but are considered to be a good predictor of quality in general. Consumers use and value this collective reputation as a source of information. Shapiro described how consumers form rational expectations on the quality of experience goods, like wine, based on the quality of

goods produced in the past (Shapiro, 1983) and, thereby, underlines the importance of reputation.

Even though the empirical evidence indicates that reputation effects are larger than effects of current quality, current quality has also an indeed small, but significant impact on the price. The reason why both, reputation as well as current quality, are determinants of price is presumably the fact of different actors on the market and that some of these actors have more information about wine than others.

Due to the importance, both of current quality and reputation, it is vital for any company to focus on all information specifications (Landon et.al., 1998).

#### *Hedonic Prices*

In their 2003 study Schamel and Anderson estimate hedonic price functions for premium wine, differentiating implicit prices for sensory quality ratings, wine varieties, and regional as well as winery brand reputations (Schamel et.al., 2003) and, thus, look into the interdependency of reputation and price in more detail. Furthermore, they examine the effects of collective reputation, as grape varieties and regions, as well as individual reputation, e.g. brand reputation.

Thereby, this study delivers further insight into the dimensions of quality and into the framework of quality.

Generally hedonic price analysis relates the price of a product to its utility-generating characteristics. As a result, any qualitative and quantitative factor that has an effect on the consumer utility can be included in the hedonic price function. By following this conventional hedonic model Schamel and Anderson suggest that a bundle of quality indicators defines any premium wine and, by that, the consumer willingness to pay is a function of that specific bundle of quality attributes. Their hypothesis is that consumers, who are uncertain about the true sensory quality of a particular wine, adjust their willingness to pay by using expert ratings of wine quality, vintage, and of producers as well as their own perception of regional and varietal reputations (Schamel et.al., 2003, p. 361). Other studies have also included more variables, e.g. aging potential, size of the winery (Oczkowski, 1994), but the findings of Schamel and Anderson on the Australian and New Zealand wine market

were consistent with earlier studies (e.g. Schamel, 2000 & Oczkowski, 1994).

They prove that ratings by wine writers and wine experts appear to influence the willingness of consumers to pay higher prices for premium wine significantly. Additionally, these consumers consider the collective reputation of varieties and growing regions when deciding on a purchase. Schamel et.al. are also able to show that wine buyers gained confidence in their own ability to recognize quality over the years and, thus, the education level of the consumers of premium wine has increased over the last twenty years.

This chapter described the interdependency of quality, reputation and price on the wine market. But wine quality still remains complex and difficult to describe. Therefore two approaches to conceptualize wine quality were presented by the author, *Extrinsic and Intrinsic Quality Dimensions* and the *Quality Framework* with its two distinct dichotomies – objective/ subjective and relative/ absolute - to be able to restructure the quality term.

*Individual and Collective Reputation* was introduced as experienced and, thereby, also expected quality, which significantly affects the price. Moreover, high reputation suggests high quality anticipation and legitimates by that high prices on wine. Finally, the hedonic price model bundles quality indicators to define any premium wine.

#### *Value Construction*

Consumers, especially when they are inexperienced, are looking for information and guidance before purchasing a product. Information plays an important role in particular on markets dealing with experience goods, whose quality can rarely be ascertained before the actual consumption of the product (Nelson, 1974 & Hadj Ali, 2007). As previously described, quality, price, and reputation affect each other interdependently and deliver information regarding the product.

The following examines the institutions, which decide what kind of wine is good and define by that, what constitutes high-quality wine.

Secondly, the mechanisms, which are responsible for the creation of trust and the minimization of uncertainty, are analyzed.

### *Wine Rating*

“An individual quality indicator (...) as a classic wine rating assigned by wine critics may also affect buying decisions” (Schamel et.al., 2003, p. 361).

Expert ratings and opinions of critics matter in many markets; e.g. the art market and the music market. These opinion leaders set up rankings, guides and competitions and, in that way, have a significant effect on consumer decisions (Schamel et.al., 2003 & Ginsburgh, 2003).

The most influential wine experts in the countries covered by this article are James Halliday in Australia and Robert Parker in the United States. Halliday’s annual released *Wine Companion* is the bestselling guide to wineries and wine in Australia (Halliday, 2011), while Robert Parker probably is the most influential wine critic in the world. Parker’s bimonthly journal *The Wine Advocate*, his wine reports, and his wine books have a direct influence on wine prices (Hadj Ali et.al., 2008). “Good grades (from Robert Parker) (...) cause prices to rocket sky-high, while, inversely, very bad grades may leave wines practically unsalable unless their prices are adjusted downwards” (Hadj Ali et.al., 2008, p.158).

Hadj Ali et.al. proved the *Parker Effect* in measuring the effect of his oenological grades on Bordeaux wine prices.

They showed that the opinion of the famous wine expert is very important for highly graded wines (Hadj Ali et.al., 2008).

Another example for experts rating wine quality is represented in the Australian wine show system. The first major Australian wine show was held in Sydney in 1850. In a wine show wines from different producers compete for bronze, silver and gold medals. In the past these medals and trophies mostly had a symbolic value and encouraged the producers to create high-quality wine, but, as the demand for premium wines grew, the medals were also of economic value as they indicated quality and, thereby, legitimized higher prizes and contained competitive advantage. So, as the Australian wine industry grew, wine shows became important distinctive events (Allen et.al., 2010, p. 37).

Today wine shows follow an elaborate rule setting and well-organized procedure to review wine. A panel of independent, knowledgeable, and skilled

judges tastes the wines blind in different classes of variety and type. Every judge rates the single wines by assigning a numeral score for different quality categories, like color, bouquet, and taste. Fixed thresholds define which wine deserves to get a medal (Allen et.al., 2010, p. 37).

As Schamel and Anderson showed, consumers frequently rely on quality signals when they decide whether a specific wine is appropriate for their individual taste and budget (Schamel et.al., 2003). Thereby, producers use their good results in wine shows as well as positive reviews of wine critics to promote their wine. Ratings, wine show awards, and trophies are strong indicators for wine quality and, especially, the wine show results are perceived as more *evaluative certifications of quality*, because they result from a structured consensus rather than one single opinion (Allen et.al., 2010, p. 39).

Allen and Germov identified the characteristics of the wineries that rely on wine shows to prove the quality of their wine (Allen et. al., 2010).

They showed that especially those wineries that produce more than 50,000 cases a year are much more likely to participate in wine shows than those wineries that produce 10,000 cases or less. Furthermore, the majority of large wineries enter their wines into more than one capital city wine show (Allen et.al., 2010, p. 43).

Besides, Allen et.al. examined the cultural impact and looked especially at the level of agreement between the results of different wine shows and whether there is a consensus between the judges or not.

Due to the absence of an objective standard, the judges have to agree on the quality of a particular wine. This *intersubjective agreement* is the main criterion (Allen et.al., 2010, p. 48). Allen and Germov found a moderate level of agreement demonstrated by the judges across diverse wine shows. The most agreement was found on the question whether a wine deserves a medal or not. Acceptable differences in the wines, due to climate, winemaking or style, cause controversy. The discussion about the importance of typicity against originality still continues among experts (Teil, 2001).

Nevertheless, the analysis demonstrates that symbolic value can be transformed into economic value. Wine producers, whose wines have been

awarded with trophies or medals, are able to charge more for these wines (Allen et.al., 2010, p. 49).

#### *Value Creation, Uncertainty and Trust*

The symbolic value created by wine writers, critics, wine shows, and other authorities influences the economic value of wine significantly. This section takes a step forward and explains how symbolic value of ultra-premium wine influences taste and examines the mechanisms that create value, reduce uncertainty and build trust on the wine market.

As described previously, institutions rate quality and, in that way, inform customers about the product, influence reputation and have a direct effect on prices.

Again, wine is an experience good, whose quality is hard to measure objectively. A certain level of expertise is necessary to evaluate the quality of a wine, even the intrinsic, gustatory dimensions of quality (Ballester et.al., 2008).

Describing a wine is difficult and often a question of vocabulary, rating a wine is more difficult and to justify a rating is even more difficult. Due to that consumers are dependent on information about the product, in order to make their purchase decision, based on the utility or expected benefit related to that purchase (Beckert et.al., 2004). Similar to the hedonic price model, every rational actor considers all possible information to be able to finally decide which opportunity promises the most benefit for him (Becker, 1993). On the (wine) market this information is delivered by collective actions of institutions and groups that possess the necessary cultural and professional authority (Bourdieu, 1984).

As earlier described, experienced quality leads to expected quality and, by that, creates reputation. Reputation legitimizes higher prizes. But economic theory of price building on the basis of supply and demand is not able to explain the extreme prices on some markets (Velthuis, 2002). On the premium wine market, which is in that case similar to the art market, buyers are confronted with the problem of uncertainty about the product quality and value. Furthermore, since markets only develop under at least conditions of bounded rationality, this uncertainty has to be reduced (Beckert et.al., 2004, p.34).

The hypothesis of this study is that the (symbolic) value of wine and, thus, the reduction of uncertainty, are not created by strictly economic factors, but by institutions within the premium wine market. In addition, the wine quality results from an *intersubjective process of rating and awarding reputation* by experts and institutions in the special field of wine (Beckert et.al., 2004 & Bourdieu, 1999). Furthermore, the producers are as important as the experts in the value creation process not only by producing the wine, but mostly by portraying their specific business model and values to the consumer and, in that way, also create trust and reduce uncertainty (Beckert, 2002).

#### *Profit- vs. Quality- Orientation*

A recent study examined the influence of motivation of winery owners in California to analyze the effects of different motivation levels on quality and price. Scott Morton and Podolny criticize in this study the Neoclassical Model (Vehlen, 1900) , which assumes that companies supply those goods and services demanded by consumers, by saying that producers have preferences about what to supply and that markets are not only demand-driven. Due to these producer preferences, products might deviate from consumer preferences and lead, thereby, to a lower rate of financial return, which is accepted by the producers, who gain “utility from certain characteristics of the product or production process” (Scott Morton et.al., 2002, p. 431).

In their model they differentiate between *Profit- and Utility-oriented* producers. By examining the attitudes of winery owners towards their firm and product Scott Morton et.al. discovered that utility-oriented owners charge more for their product on a quality-adjusted basis and are mostly located at the higher end of the quality spectrum. In contrast, profit-oriented owners are less likely to produce high quality wine (Scott Morton et.al., 2002).

Dilger proved these findings of Scott Morton et.al. in his study on different management configurations in the German wine industry (Dilger, 2009). He showed that different management configurations have distinct effects on the performance of a winery.



The wine market is mostly defined by monopolistic competition. “There is not one price for all wines or just for each given quality of wine. Instead, there is an interaction of quantity, quality and price for every single producer” (Dilger, 2009, p.200). Generally, an increase in production lowers the enforceable price, while an increase in quality raises the price. An increase in quantity as well as in quality escalates the production costs. Dilger showed that utility-orientation correlates with quality, while profit-orientation mostly comes with high quantity and lower quality (Dilger, 2009).

According to these findings, chances are supposed to be high that winemakers and owners of ultra-premium wineries are utility- and, thus, quality-oriented.

### 3. RESEARCH QUESTION & METHOD

Ten wineries from Australia and ten wineries from California were selected to represent the premium red wine production in these New World wine producing areas (Table 1). The wineries were chosen based on recent rankings, classifications and expert ratings (Johnson, 2009; Langtons.com, 2012 etc.) and contacted via telephone and email. Only highest rated, outstanding wineries, which regularly produce wines of exemplary quality and typicity were selected to be part of this study. Furthermore, as soon as the winemaker agreed to participate and the organizational circumstances allowed visiting the winery during the time frame of the interview study, the winery was included in the sample. This method led to a (partly) random selection of the wineries.

Finally, ten wineries were visited for personal interviews with the winemaker in Australia and eight wineries were visited in California. Additionally, two interviews were made on the telephone with Californian winemakers. Table 1 shows the characteristics of the wineries of the sample set.

The standardized interviews lasted from 30 to 120 minutes depending on the elaborateness of the interviewee to test the following hypothesis:

1. Institutions and mechanisms of reputation are value creating factors on the wine market. Quality is, by that, socially constructed.
2. Wineries influence, with regard to their resources, this quality creating process actively and independently.
3. The wineries influence the value creating factors significantly by active profiling.

#### *Resources and Capabilities*

All participating wineries are generally small, boutique-sized to medium-sized companies, which either grow grapes on their own property and/ or purchase grapes from long-term relationship growers. They all produce and sell wine out of these grapes. The total production differs from 750 to 60,000 cases annually, with one winery being an exception with a significant larger production of 350,000 cases of wine each year (see: Table 1).

Furthermore, the most relevant differentiating factors for these companies are the vineyard sources and the grapes these vineyards produce. It is widely agreed that the terroir, including the vines, the vineyard, the climate etc., heavily influences the quality of the fruit and, by that, the quality of the wine (Sykora, 2012).

Code	Appellation	Production <sup>1</sup>	Price of Flagship <sup>2</sup>
AU01	Coonawarra	10,000	94,5
AU02	Barossa Valley	8,000	105
AU03	Barossa Valley	19,000	84
AU04	Eden Valley	30,000	630
AU05	Clare Valley	2,000	63
AU06	Barossa Valley	60,000	735
AU07	McLaren Vale	2,500	31,5
AU08	Hunter Valley	350,000	84
AU09	Hunter Valley	6,000	63
AU10	Hunter Valley	35,000	63
CA01	Sonoma County	25,000	90
CA02	Santa Cruz Mountains	3,000	175
CA03	Napa Valley	65,000	120
CA04	Napa Valley	4,500	90
CA05	Napa Valley	750	750
CA06	Santa Cruz Mountains	4,000	60
CA07	Sonoma County	5,500	85
CA08	Sonoma County	7,000	65
CA09	Sonoma County	3,000	60
CA10	Napa Valley	32,000	225
Ø		33,500	184
m		175,375	390

<sup>1</sup>Annual production in cases

<sup>2</sup>Most expensive bottle in the product portfolio in US Dollar

**Table 1:** Characteristics of the wineries of the sample set used in this study

There is a link between the reputation of a vineyard, the fruit it produces and the value of the grapes (Laube, 2012a). Thereby, it is a key advantage that all participating wineries own or buy fruit from premium vineyard sites.

Moreover, every Appellation has a strong reputation and is very well-known for producing high-quality wine. The wineries in this sample all gain profit from this matter of collective reputation.

All wineries have a well-established distribution network and sell most of their wine domestically, but also distribute wine all around the world.

The winemaking creates- together with the core strength resulting from the high-quality vineyard- a strong organizational capability with potential for

creating a significant competitive advantage in all participating wineries (Grant, 2003, p. 131).

Innovation, even though it is not essential, does take place in the winemaking process and in the viticulture, but research and development is generally not important to thrive on the market. The participants work with traditional winemaking methods in the winery and have a strong focus on quality.

To summarize, the resource-based evaluation of the wineries participating in the survey and their capabilities show clear core competencies, which are able to constitute a feasible and successful strategy and sustainable competitive advantage (Prahalad et al., 1990, p.91).

Firstly, the highly acclaimed vineyards located in premium appellations in Australia and California deliver the main resource of the wineries. In combination with the capability of high-quality, skilled and experienced winemaking the vineyard sites show their full value. Besides, the scarce source of fertile, high-quality vineyards yields high returns even on competitive markets (Grant, 2003, p. 128).

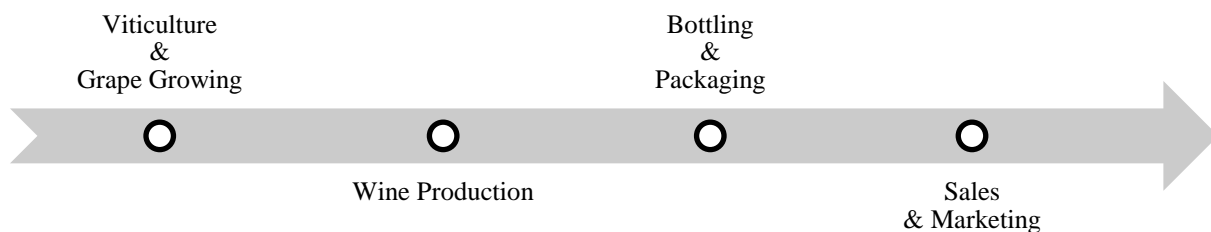
*Value Chain*

Developed by Michael Porter, the value chain concept describes the series of value-adding actions, from raw material inputs to the

consumption of the finished product, within a company (Porter, 1998). This series consists of primary activities, which are directly related to manufacturing, and of secondary activities, which support the primary activities; e.g. Research and Development (Fearne et al. 2012, p. 276).

Value chain thinking provides the enabling business environment- analogous to the resource- and knowledge-based approach from chapter 6.1. in this thesis- for the creation of sustainable competitive advantages (Conner et al. 1996, p. 476 & Hopkins, 2009, p. 46).

The value chain of the wineries participating in the survey is displayed in the following figure:



**Figure 3:** Value Chain of the Wineries

*Viticulture & Grape Growing*

The wine industry - especially small, boutique-sized businesses - is strongly connected to weather, seasons, and general growing conditions throughout the year, because it depends on the grapes from the vineyard as its agricultural produced raw material. Big industrial wine producers are also dependent on their grape sources and thereby the growing conditions, but these producers have more vineyards, which are often located in different regions or even states. By this diversification, the big producers are able to reduce their risk of a single bad harvest with low yields.

As most of the wineries in the sample are small to medium-sized producers which source their grapes only from their estate vineyard, they are highly dependent on the vineyard performance. Even though, research and development does not play a crucial part in the value chain of the wineries and is thereby not displayed among the main segments of the value chain. Nevertheless, every element of the value chain involves aspects of research and development on a micro level to keep up with the latest trends and improvements. As described

earlier, the vineyard is the most important resource of all sampled wineries.

Compared to many of their competitors the participating ultra-premium wineries have superior vineyard sources and try continuously to improve the performance of their vineyards and their vines by traditional, sometimes biodynamic, as well as modern viticultural techniques.

*Wine Production*

The essential step in the value creation process is the transformation from grapes into wine, of course. Even though, the fact that winemaking is generally a simple and well-known procedure, the production of high-quality, world-class wine is very delicate and complex.

Compared to their competitors in the ultra-premium segment of the market, all participating wineries have at least as competent winemaking and vineyard management teams as their competitors, which enable them to produce consistently higher quality than most actors on the market.

Following the vineyard source, this area is crucial for differentiation and creating competitive advantage. It is very important for all wineries in

the sample to maintain this core competence bundle on a high level for the future to thrive on the market. Thereby, it is one of the biggest challenges to preserve the knowledge of the winemakers for the upcoming decades.

*Bottling & Packaging*

While bottling and packaging of the wine is not a differentiating factor, it offers possibilities for cost savings and efficiency.

Three main components are involved in this segment: Cork, Bottle, and Label.

All Californian producers use natural cork for their products. Since the American consumer expects cork as a closure on ultra-premium wine bottles, nobody has changed to different closure options; unlike most of the sampled wineries in Australia. The wineries, which use cork, are very picky on choosing their specific cork producer. Often the winemaker is personally involved in the bottling process and in the testing of the corks prior bottling. The Californian producers only buy high-quality cork to minimize the chance of any cork faults or cork taint. In addition to that every cork is checked individually in the winery. Interestingly, most of the sampled wineries in Australia turned cork down and use substitutes, like screwcap or the VinoLok closure, now.

Compared to the natural cork closure, the bottle and the label are generally less delicate. Furthermore, the bottles as well as the labels are less relevant for

quality perception and sales (Economist, 2012). When it comes to the bottle, it has to fulfill certain functions as protection of the wine, stability, and transportability. As long as these requirements are fulfilled, there are chances for cost reductions. The glass does not affect the wine and the heavier the bottle the more expensive the logistics and shipping costs are.

It is similar with the labels, which have mostly informational character and are not responsible for a differentiation on the market. Labels or label designs do not effect buying decisions on the ultra-premium wine market (Economist, 2012).

*Sales & Marketing*

Wine consumption has been decreasing over the past two decades and the pressure of globalization grew at the same time on the producers (Anderson, 2003, p.659). Even though the small to medium-sized producers on the premium market do not feel the pressure as much as the large volume producers, it still remains important to stay present for old and possible new customers. The feasible ways to market and sell wine are also part on the following empirical section.

*The Survey*

The standardized interview contained the four main items, including resources, quality, business model, and profile to test the hypothesis. Each main item was operationalized as in Table 2.

<b>Resources</b>	<b>Quality</b>	<b>Business Model</b>	<b>Profile</b>
Core Values	Definition	Markets	Corporate Identity
Geographical Impact	Quality Factors	Globalization	Market Influence
Product Portfolio	Authorities	Sales Channels	Restrictions
Price Segment	Expert Ratings	New Technology	Product- vs. Demand Driven
History & Tradition	Wine Shows	Grape Origin	Reputation
Infrastructure	Blending/Single Vineyard	Profit- vs. Utility Orientation	
	Cork vs. Screwcap		

Table 2: Disposition of the survey

## 4. RESULTS

This chapter summarizes the statements of the different winemakers regarding the diverse items of the standardized questionnaire.

### Resources

The following section reflects the results from the first part of the questionnaire, which aimed at the resources of the wineries and how the winemaker pictures the situation; including core values, reputation of their appellation, product portfolio, price segment, importance of history and tradition, and rating of their specific level of provision of infrastructure.

#### Core Values

When asked about the core values of their winery, the winemakers answered with high consistency in referring not only directly to the company, but also to the product and the characteristics of the wine. History and tradition were mentioned by 15 of the 20 winemakers among the core values. Whether it was the maintenance of tradition in general as a core value of the winery, or the reference to a long history, heritage, pedigree or family tradition, tradition is one of the key core values.

Additionally the connection from vineyard to wine was emphasized. With the wines as *an expression of terroir* (AU01), *superior grapes and wine* (AU04), *estate grown wines of site* (CA02) or with the *philosophy (...) to produce genuine and authentic wine representative for our own (...) vineyard with minimal input in a traditional way* (AU02), the link to the vineyard and the grapes seemed to be of great importance. The quality aspect was mentioned- often in connection with quality dimensions of the wine- among the core values as well. *Quality is number one priority (...). We need to make a wine here that is among the highest quality in the world* (CA05).

Some winemakers already went into detail describing their image of a high-quality wine as *distinctive Australian with a European influence* (AU01), *fairly Eurocentric wines* (CA06), ageable, elegant, and balanced were descriptions used amongst others.

Another core value seemed to be the commitment to nature as well as to society. *It is respect for the*

*people that work with us and the community* (CA10), *being a good neighbor* (CA05/ CA10), *care for the people and the employees* (AU04) and sometimes *commitment to the local community*, too (AU01). The high frequency of these values represented the high integration of the wineries in their local society and environment.

To summarize, the four main areas represented among the core values of the wineries in the sample were the importance and presence of history and tradition, the strong link between vineyard and wine, the quality focus, and the integration into and the commitment to local society and nature.

#### Geographical Impact

Three main perspectives on the value of the wine region can be observed. Firstly, the connection between region and grape variety seemed to be important. *If a winery in a region is making wine from a variety in accordance with the tradition of the region then you can anticipate* (AU05). To give some examples, the Napa Valley's reputation is founded on the good performance of the Cabernet Sauvignon grape over the years, while the Barossa Valley became famous for its good conditions to grow Shiraz. Thereby, many winemakers reviewed the value of their region not only on its actual reputation, but explained the reasons for the actual status. Since all twenty wineries of the sample are located in regions, which enjoy a very good reputation on the wine market, the chances were high that the winemakers would acknowledge this aspect, which they mostly did. Twelve winemakers punctuated the growing conditions for their varietals and praised their micro-climate and terroir. Tradition and history were valued as quality indicators for a region. *Coonawarra does have a good reputation, because it is a longly standing region* (AU01).

The collective reputation connected to the appellation was regarded positive by most of the winemakers.

The two winemakers and owners of wineries located in the Santa Cruz Mountains Appellation underlined the long history and great growing conditions of their AVA (American Viticultural Area), but admitted that the region's reputation is not as strong as the reputation of the Napa or Sonoma Valley.

The level of tourism as a special feature linked to the region was brought up, by the winemakers in the Hunter Valley, who have the *busiest cellardoor in the country* (AU10).

There was a high level of agreement that the collective reputation of a region supports the sales, but also critical statements showing that the Appellation is a crucial quality indicator, but not a sufficient factor. *At the end of the day a winery that produces lesser quality can put the same appellation on the label as we do* (CA02).

Furthermore, the embeddedness of a region also reflects in the function of the country's reputation as a wine producing nation. *Our reputation is to some extent tied to Australia's and Australia is a hard place at the moment* (AU07).

#### *Product Portfolio*

While the core values as well as the numbers represented in Table 1 show many similarities between the participants of the study, the product portfolios differ significantly. Some sampled wineries have only one product for sale, while others sell more than 20 different wines - and that even excludes AU08 with more than 40 different wines in their product portfolio. Generally, the smaller the annual total production, the smaller the product variety is. All wineries, which charge significantly different prices on their products, do have an outstanding, flagship wine – a product which they are especially well-known for. The wineries with similar prices on their wines in the portfolios do not usually have this kind of single product of importance.

#### *Price Segment*

The covered price segment also spans a big range from 20 USD to 750 USD per bottle. All winemakers agreed though serving the ultra-premium, luxury segment of the wine market. The cheapest flagship wine of a product portfolio costs 30 USD, while the three most expensive single bottles cost 630 USD, 735 USD, and 750 USD. The earlier illustrated relationship between price, reputation, and quality, is not able to explain these extreme differences in pricing. Other emotional factors, like prestige and scarcity, seem to be responsible (Hooke, H. 2012b). *The pricing is*

*partly based on cost of production, but more on supply and demand* (AU09).

Broader product portfolios with affordable everyday wines help *to have your label up in the presence of your consumers* (AU04), while most of the participants aim at the *knowledgeable wine-drinker* (AU01), *gain very much towards the high-end consumer* (AU06) and target the *more than averagely interested consumers* (AU07). *We cannot compete as a winery of our size in the lower portions. You can find our entry level wines in a bottle shop ranging anywhere from 17 to 22 AUD. And that is what the wine world calls premium* (AU10).

Value for money is an important issue for many of the winemakers in the sample. *We are not eye-catching expensive, especially giving our reputation. But I have always been somewhat democratic in my view on wine pricing. I do not need to have super-high pricing to get attention to the wines. And I would like to offer, even at 60 USD a bottle, a feeling of good value* (CA06). This solidarity to the customers, especially to long-term, mailing list customers, can be observed at several wineries.

#### *History & Tradition*

*For us (history and tradition)(...) is very important. And that is one of our points of difference. You look in the winery and you see all that old equipment. It is not a museum, we actually use it. That is the difference and part of the whole thing. When you walk around the courtyard here, people can see what we actually do.*

*The public can watch the whole process during vintage, see the old equipment work. That is incredible marketing* (AU03). *Having a successful history is a quality indicator. Especially from a marketing perspective* (AU02).

All winemakers strongly agreed on the importance of history and tradition in the winemaking process and listed several arguments. Especially Australian consumers seemed to appreciate aspects of history and tradition in wine marketing and advertising, but the most frequent argument pro history was the learning curve and the experiences gained over the years.

Thereby, tradition and history are hugely important in viticulture as they are *in any agricultural pursuit (...) where (there) is a multigenerational learning (...). There is a lot of knowledge about the soil and what grows best where. It sounds simple, but it is really important to have a successful vineyard (AU04).*

*The reason that some of the vineyards in Burgundy are so great is that some of them are on their third, fourth, sometimes fifth generation plantings. And, with access to multiple vintages, and experience you figure out what might work best in that particular spot. These little adjustments that you make are critical and the knowledge only comes with time (CA01).*

Next to the viticultural aspects and, thus, the best possible fittings between terroir and varietal, which were established over years of experimenting, winemaking techniques and methods in the winery are a result of long-term development as well. Californian and Australian winemakers often refer to Old World examples and standards using the longer history and specialization of European, mostly Burgundian and Bordeaux, winemakers as an example for high quality. *In the winemaking process we use Old World techniques (AU01). So my influence is heavily a Burgundy influence, but I am not trying to make Burgundy wines. I am making (...) (our) wines, but with very traditional methods (CA07).*

Even though, the New World wineries have established their distinctive products and wine styles, the Old World still seems to be the benchmark; especially the wine producers from Bordeaux and Burgundy, which dominate most expert ratings and wine lists around the world.

*History is very important, but you always have to keep looking forward as well (AU08).*

#### *Infrastructure*

Infrastructure did not seem to be an important differentiating factor. All participating winemakers were satisfied considering their level of provision of infrastructure. *We are completely over equipped. We are luxuriously equipped given our size. We are in the fortunate position where we can get everything we think we need (...). But we still do things in exactly the traditional manner (AU05).* Most winemakers put more emphasis on traditional

methods and, thereby, commented ironically on state-of-the-art equipment. One consensus was that you do not need fancy, highly technical equipment, but it sometimes makes things easier.

*I think Napa Valley is higher in those aspects, because most of the people here make high-quality wine. We all have basically the same technology. People like Opus One and ourselves, we are the ones starting stuff; like the optical sorter (...), and people follow right behind.*

*You do not see a lack of technology here as much as you would outside; say in Anderson Valley where you see the mums and pops standing in the barns like always. They do not have the profits to reinvest into their infrastructure. We have always reinvested in our infrastructure to keep up with the quality (CA10).*

#### **Quality**

Wine quality is a complex construct which is tough to define. With the concepts of a Quality Framework as well as Quality Dimensions this section structures the answers of the winemakers relating to quality.

#### *Definition*

*Yes, what is quality...Yes, maybe I should come back to that question... (AU05).*

*It cannot be defined. I read a few books on that philosophy. I do not think you can define it, because it is something that the individual perceives. Certainly perceptions can be different, but it is about not letting anything else influence the end product, not compromising, remain focused and being true to your core philosophies to deliver a product that you perceive as quality (AU06).*

The question for a definition of quality led to most controversy among the winemakers. Every winemaker had his personal view on what quality meant to him, but at the same time they all agreed on the complexity and on the fact that it is impossible to agree on a single, absolute definition.

*It is probably a lot of things. I think in wine it is based on a product being a reflection of the variety, the place and the producer in a particular season and then captured in a bottle. You cannot upscale that (AU07).*

*But then you get to a point of where you have wines that are all very good wines and that is where marketing and the subjectivity take over (AU01).*

Certain aspects can be judged objectively, like varietal correctness, but influences of the vineyard and the season cannot be measured or predicted. Additionally, quality is collectively (subjectively) measurable, e.g. by a level of agreement of wine judges following standard values in a wine show. But even under these circumstances individual taste and subjectivity take over at a certain point.

*It is about how every wine that you make looks and how consistent they are across the line (...). Quality is not that perceived sameness, because our wines are not the same every year (AU03). It is pretty subjective, and that is what it makes so difficult. It is very variable (...) and the whole way how wine is sold and presented celebrates that variation. Beer for instance is all about consistency (...).*

*Wine is about exploring differences; regional differences, vintage differences. So it is less about meeting particular color and tannin levels, but still there is a certain amount of consistency that is expected from a region or producer (CA08).*

Ironically, variation was supposed to be a quality indicator, as the winemakers wanted their wine to be a reflection of the vineyard and the seasons over the year.

*Quality is the whole package and not just this subjective measurement of what we put in the bottle. Unfortunately there is not a machine that you put a drop of wine into and it gives you a quality score (AU09).*

*Our business has a great amount of subjectivity in it. I think as a good part of wine quality is similar to art or other fashion industry items where the definition of quality is as a foundation in measurable and perceivable aspects, but has layered on top of it a lot of image and reputation (CA02).*

*One thing upfront, it is definitely not power equals quality. For me it is a lot more sophisticated than that (CA03).*

*Quality has a couple of components. Component one is having a vineyard site that makes grapes that are inherently very pleasurable (...). I view winemaking as more as a quality preserving activity than a quality producing activity. The*

*quality is in the fruit and our job is not to mess it up (CA05).*

The level of agreement was very high on the importance of the vineyard and the fruit quality resulting from all aspects of the terroir. In addition, the multidimensionality on the dichotomy levels of subjectivity and objectivity were validated.

*Quality is clean, varietal correct, complex and seductive aroma with balanced acid and tannin. Those are kind of easy to obtain, but probably the most important thing that really makes quality to me is the backend of the wine (CA06).*

*For me the quality of a wine is the first impression of the glass, that purity, energy, liveliness, beautiful aromas, perfume, something that draws you in (CA07).*

*A winemaker's idea of quality is just in the glass (AU08).*

All quality variables that were mentioned by the winemakers in this section are displayed below. The intrinsic, subjective factors seem to dominate the quality construct. Additionally, the objective parts are considered to indicate quality prior consumption of the end product, while the subjective aspects are perceived when experiencing the wine:

#### Objective Quality Dimensions:

- Old Vines <sup>1</sup>
- Quality of Oak
- No Additives
- Absence of Faults
- Color <sup>2</sup>
- Turnover in Secondary Market
- Price
- Ripeness
- Alcohol
- Acidity
- Varietal Typicity
- Traditional Winemaking

#### Relative Quality Dimensions

- Structure
- Flavor
- Complexity



- Perfection
- Value for Money

#### Subjective Quality Dimensions

- *Balance*
- *Tannins*
- *Length*
- Customer Perception
- *Drinking Experience (Smell, Taste etc.)*
- *Pleasure*
- *Fruit Intensity*
- *Oak Integration*
- Ageability
- Reflection of the Vineyard
- Reflection of the Vintage

<sup>1</sup>In black: Extrinsic Quality Dimensions;

<sup>2</sup>In italic: Intrinsic Quality Dimensions.

#### *Quality Factors*

To add more facets of quality to the framework, this part of the survey aimed more specifically at single quality indicators. Many aspects already represented in the section before were proven in this part as winemakers underlined statements that other winemakers made earlier and vice versa. Hereby the significant importance of the vineyard source was one example.

*There are factors indicating the quality like the vineyard or the grapes (...). I see our wines as that authentic natural quality. It comes from the vineyard directly into the bottle without additives (AU02).*

The subjectivity and taste of each winemaker heavily influence the product. It is the palate of the winemaker which defines the benchmark of the wine he produces.

Wine experts are not superior tasters, but their approach to wine assessment using previous experience and possible normalized references to assess concepts differ (Hughson, A. 2008). Furthermore, similar to the earlier presented influence of the involvement levels of consumers in their approach to wine (Charters, S. et.al. 2007); experience and knowledge about wine seem to affect the individual perception of wine quality.

*In any art form the experience and the knowledge of the viewer is everything. If your taste in music is rap and you hear Beethoven... (CA06).*

The consumption of wine was often compared with an experience, similar to the experience of art or music, which is always personal and, thereby, subjective. *Wine is a drink, an alcoholic beverage. Everyone's opinion and everyone's taste are physically different. There are a lot of emotions going on and preconceptions that affect your view of quality. That is really complex. I can be very technical about it from a winemaker point of view, but if you go to the next step and to other people's view on quality then you get different opinions. I just think it is personal (AU08).*

Emotions seem to affect anticipation and, thus, the perception of wine. Wine consumers tend to be influenced by trends and expert opinions.

Tastes are different and, thereby, hardly a standard for quality, but there are factors, like structure, richness, and complexity that increase the chance for a consensus and a higher level of agreement, whether by consumer or critics, that a wine tastes good.

*A simple quality wine has no faults, it is delicious, enjoyable and consistent (in taste), but really quality wines are complex. When it is young it is a certain way and then you open it over a course of two or three days and it is changing and revealing layers. Over the course of years it changes and shows different cores of quality. To me that is really important (CA04).*

*Structure is important. It makes the wine age well. Structure is something that you cannot measure, because it is basically how the wine interacts with itself. So the fruit, the oak, the acidity, the alcohol, the overall balance in the wine (...), the mouthfeel, the aftertaste and the pleasant experience play a role. Even though you cannot measure that, it is a quality indicator (AU09).*

*Our ideal profile is going to be a wine that has flavor and personality (CA08).*

To summarize, as the winemakers reflected the quality term again, the focus went more to the subjective aspects and quality indicators. The importance of the vineyard source and the grapes was underlined as well as the importance and influence of the winemaker. The personal style and

taste of the winemaker seems to influence the end product significantly.

Additionally, the wine itself was described with mostly subjective, intrinsic variables as complexity, structure, personality (of the wine), and ageability.

Besides, the importance of the situation and characterization of the wine consumer himself was emphasized. Factors as the proximity to wine, the expertise and knowledge about wine, and the wine education of the consumer affect the quality experience as well as the individual, emotional setting of the consumer.

#### *Authorities*

All winemakers acknowledge the influence of different authorities on quality perception on the premium wine market and how these authorities influence the buying behavior as well as general trends in production.

*The whole Robert Parker phenomenon is the most extreme example (...). If Robert Parker gives one hundred points to your wine, it is sold out tomorrow and you can ask for whatever price you like for it (...). Some winemakers make wines that Robert Parker likes and aim at specific markets. That syndrome is an expression of how powerful Robert Parker is (AU01).*

Very few critics have a strategic influence on the world market, but a whole network of authorities spans the market and covers all niches. Wine writers in local and regional newspapers are considered to influence mostly infrequent drinkers, who do not read wine magazines, like Wine Spectator or Wine Companion, which generally have a strong influence.

*The media for sure. The media and tasters online now. There are a lot of tweeting and online comments that people really follow. So that is quite an interesting assessment (AU04).*

The new media is considered to create a shift in authority from the critics towards the consumers. Wine blogs and forums, where consumers share their experiences about wine, are growing and, thereby, the consumers' independence increases.

Other important institutions seem to be the buying agents for supermarkets, who are considered to be gatekeepers deciding whether a certain wine is available for customers or not. Sommeliers and restaurateurs play an important role especially in

the ultra-premium segment of the market, where consumers expect the presence of a brand on the menu of the world's best hotels and restaurants.

But besides the critics, the producers seemed to have a strong influence on quality perception on the market as well.

*We (...) do a lot of wine education and wine dinners. For me, that is a great way of defining quality in the market (AU06).*

*I think it is very important for the producer to portrait his brand at a certain level of quality. And I think the best way to achieve that is third party endorsement. For me it is to get across all the different critics to reach all the different demographics. The more critics agree on your wine quality, the better (...). I like my business model where I do not spent much at all on advertising and marketing (AU09).*

#### *Expert Ratings*

*Ratings obviously influence sales (AU04). The experts are important. They helped us establishing the new brand. We got and still get some good ratings from James Halliday and others which make us aware to the consumers (...). Ultimately it is the consumer. The experts are important, especially for the initial decision. Some consumers need the reinsurance from experts (AU02).*

Similar to the responses in the foregoing section, all winemakers agreed on the importance of critics for defining quality on the market and how they affect sales, but all winemakers had the same opinion that these critics do not affect the way how they produce their own wine. The only exception in this sample was one winemaker approving the influence of critics and trends on the way the wine is produced for the commercial tier of his winery, while the premium level remains unaffected by critics' opinions or market trends.

*Internationally Robert Parker had a very significant effect on Australian wine; particularly the big alcohol syrupy styles that he likes. And that has made a lot of people particularly in South Australia particularly in the Barossa Valley make a lot of money, but at the same time you live by the sword, you die by the sword (...). The whole Parker syndrome got a bit of a joke in Australia (AU09).*

*Not at all (...). We have always made wine for us. It was and is our vision. But the critics have been very generous to us over the years (CA01).*

Authenticity seemed to be an important value among all premium winemakers, but the importance of critics especially for new, non-established wineries to get attention was widely acknowledged.

#### *Wine Shows*

Even though, wine producers, whose wines have been awarded with trophies or medals, are able to charge more for these wines, wine shows seemed to have lost importance on the Australian wine market. Many of the wineries in this study do not participate in wineshows anymore or do less wineshows than they did in the past. It became obvious that wineshows lost their importance, especially for established, small to medium producers.

Wineshows never had the importance in California like they had in Australia, but the general development is similar as most of the participating wineries do not do any wineshows in California (to any further extent) and, if they do, these wineshows are simple marketing events where wines are presented to a greater audience. There is hardly any structured competition or wine judgment as in the Australian wineshow system.

*We do not do that as much anymore (...). They taste hundreds of wines in one setting, and I have done that myself, there is no way... We try not to do those anymore (CA10).*

#### *Cork vs. Screwcap*

The question of the bottle closure divided the two wine countries the most. While in Australia (almost) every winemaker has replaced natural cork with screwcap or other substitutes over the last years, every premium producer in California still uses natural cork as closure for his wines.

After talking to twenty different winemakers, it became obvious that every winemaker has made his individual experiences and has his own philosophy and, thus, is following his very own logic why he is using cork, screwcap or another type of closure.

*Pro-cork performed best in the closure trials. That is why we use pro-cork with our wine at the top end, because we think these wines need air to*

*evolve properly to mature, because they are quite tannic. At the bottom end with less tannic wines we use screwcap. That retains the freshness and slows down the evolution, which is good for marketing as well. So we have a two way approach to closures and we say that there is no perfect closure (AU01).*

*Here in Australia it makes no difference. Internationally there are still some people that perceive screwcap to be cheaper and expect cork in the high end wines, but I think that attitude is changing. And from our wine quality point of view in terms of aging and no taint, I think screwcaps are definitely the way to go (AU02).*

*We believe that cork plays really an important part for aging a wine and how it develops in the bottle, but screwcap has a place, definitely. It has a place for wines that are not going to be aged and to be drunk within the first four years. Some of our wines are bottled under screwcap and anything that we have to age, we put under cork (AU03).*

*We did not just change from cork to screwcap. We changed to the Vino-Lok. We call screwcap a transition closure (AU04).*

*It does not matter how much you pay for your cork, you still suffer the same incidents of cork taint (AU05).*

*If you are in Chinese or if you are old school French, cork is a quality indicator. It is a traditional thing and it was for a company like us very hard to go away from cork- for a lot of reasons. The best wines that you have ever drunk were all under cork (AU08).*

Only two producers in the sample still used cork as their preferred closure for their products. The reasons vary, but the lack of reliability seemed to be the main argument against cork in Australia.

Most interesting for this thesis is the fact that almost all winemakers acknowledge the function of a cork closure as a quality indicator at least on some markets.

In contrast to the development on the Australian market, Californian winemakers still use cork. All sampled wineries use cork on their premium products.

*I never see a synthetic closure on our wine (...). Besides cork is necessary for the ageability (CA01). I like screwcaps for wines which are to be consumed in their early years, but in the United States and in other parts of the world, like the far*

*east, cork is still thought of to be a quality indicator- and certainly good cork (CA03).*

*Cork certainly influences the development of the wine in a bottle. A wine that is under cork, versus screwcap for instance, is typically different. And for us historically the wines have aged very very well under cork, so we, the critics and the consumers like the characters of our wines after 5, 10 or 20 years under cork (CA05).*

*It is partially cultural. In the United States cork is associated with higher quality wines and screwcap with cheap wines, but that is changing. Screwcap is very convenient and consumer friendly. As to our practices, cork is a very traditional closure and we think a lot on cork and which cork to purchase. I think the cork industry has gotten better (CA08).*

*I am a strong believer in cork. It is a natural product and it is part of our sustainable act (CA10).*

All Californian winemakers agreed on natural cork as their preferred closure for premium wine. They valued cork to be a sustainable, natural, and traditional closure, which is appropriate for their wines. Being aware of the failure rate in cork, the winemakers recognized improvements in the cork industry and, thereby, the decreasing of cork related wine faults.

Besides, in the Californian wine industry screwcaps were considered to be appropriate for cheap wines or wines that are meant to be drunk early after bottling, since natural cork is necessary for the aging process of a bottled wine. Furthermore, the winemakers agreed on the market related perception of cork as a quality indicator.

## **Business Model**

### *Markets*

The participating wineries sell most of their wine on domestic markets. While eighteen wineries also export 25 or less percent of their production to global markets, one winery in Australia and one winery in California do not export any wine at all. Considering the small total production of most of the participants and the high demand for their wines, there is hardly any necessity to approach foreign markets.

### *Globalization*

While all winemakers are interested in wine production, different varietals, and wine styles worldwide, they do not follow trends or let them influence their genuine styles.

*No, not really. There is not really a lot that affects the way; I make wine- not even the consumer preference. I make the wines I am passionate about and it is only a small amount. I am in the fortunate situation where I can make the wines that I like and that I am passionate about and there are enough people out there that agree with me and buy it. I do not chase the market (AU09).*

*No, (...) (Globalization) does not change anything that we have done. We do not make wines stylistically different for anybody anyway (CA04).*

Adaption to global trends takes only place in the lower tier of at least medium-sized wineries or when ideas for new varietals derive from markets abroad. As the demand for Rosé wines grew, some wineries produced this kind of wine, while their premium products remained unchanged.

### *Sales Channels*

All participants sell all or parts of their production directly to customers. Tasting room sales are particularly strong in Australia, and especially in the Hunter and Barossa Valley, while the Californian sales are dominated by mailing list sales.

Online sales are the fastest growing sales channel in both countries. Most winemakers do not sell their wines via supermarkets. Instead distribution on premise sales and retailers play an important role for brand presence and brand building.

### *New Technology*

New technology seems to have no direct impact on the winemaking, but – while the general techniques and methods remain unaffected – tracking and measuring processes became more convenient. In addition and in close connection to marketing and sales, information technology does heavily influence the way the wine is advertised and sold.

*It does not affect the winemaking, but having access to information and sharing information had an impact on other things. Certainly the way I buy materials and the supply are a lot different than*

*when I started. People are sharing diagrams and purchase orders all on the fly. I made a purchase order on my phone just today. In some ways IT made it easier. It had a huge impact on the way we market and sell our wine (CA01).*

#### *Grape Origin*

The sample covers the entire span of possibilities to obtain the necessary grapes for wine production; from the model with 100% estate grown fruit to businesses which purchase 100% of their fruit from independent growers. But, besides these extremes, most of the sampled wineries get the majority of their grapes from their own cultivated and controlled vineyards and just buy some fruit from growers to spread risk or to compensate cuts due to vintage conditions.

Buying the raw materials gives the winemaker more flexibility and the chance to reduce risk on the one hand, but on the other hand less control over the viticultural aspects and, thereby, the quality of the grapes.

#### *Profit- vs. Utility Orientation*

As earlier studies indicated, the levels of utility-orientation were consistently high throughout the sampled wineries.

*Just the love of making wine (CA10).*

*Money is important, but having a good environment to work is more important (AU03).*

*And as far as the financial factors go I could, if I wanted to, be more profitable (...). I could be more profitable, but it would change the nature of the business which I am not willing to do (AU09).*

*Our brief is to make the best wine and if that involves a little more cost that is fine (AU10).*

*To be honest, there is something magical about the process. Trying to capture a sense of time and place every single year. Having your life driven by the seasons and its cycle and rhythms. It is a unique intersection of art, science and commerce. There are very few industries like it (CA01).*

*The reason why we are here is the strife to make one of the best wines in the world. That is why we come to work every day (...). Money is only secondary (CA05).*

The winemakers seem to be mostly driven by the passion and love for the product and by the

production process including the diversity and independence in the winemaking process.

#### **Profile**

This final segment of the questionnaire aimed at the organizational culture and the profile of the wineries as businesses.

#### *Corporate Identity*

*That part is not so well defined. We have a small team (...). We do not consider it corporate (CA09).*

Most sampled wineries are small, family-owned companies, which do not have a defined strategy or corporate identity. The focus seemed to be quality- and product- driven. Thereby, the identity is defined by the brand and the wine.

*Not so much. We are a small family owned and founded winery. We have a handful of people working for us. It is a pretty close organization (CA01).*

*Well, it is a very small team. So when we get together we are all sitting at one table (...) and everybody who is working for the company is right there. It is only a handful of us, so communication is quite good and we avoid a lot of issues that a larger organization might face. As far as the corporate identity, again, that is the quality. That is the reason why we show up (CA05).*

#### *Market Influence*

*No, not at all. We are very lucky in that regard. We have had a singular vision from the beginning and stacked to it. And the market has managed to come to us (CA01).*

*It does in general, but not for us. The bigger guys start buying (grapes) from all over the state, when the demand grows to make more wine that sells (CA10).*

The market does not seem to have any influence on the core values on the wineries. Instead, the only effects that might occur due to the influence of market developments happen at the wineries with larger productions and in the lower product tiers of these wineries.

*I like to think that I am small enough that I can make wines that I feel are the best expression for what the wine truly is (CA06).*

### *Restrictions*

Generally restrictions that affect the winemaking barely appear at the participating wineries. As the wineries have to remain financially stable businesses, money has to be a limit for certain actions. But interestingly, this does not seem to cause any significant changes for the winemaking in all twenty wineries as the striving for quality always comes first.

*Being certified organic means being restricted what you can use in the vineyard and in the winery (...). That is the only guidelines we go by (AU02).*

Besides legal restrictions, which affect the winemaking, but do not limit the winemaker in what he wants to do, the study did not show any noticeable negative influences from the commercial area.

### *Product- vs. Demand-Driven*

*Definitely the product. It is about the vineyards that you can source from and there is only a finite amount of top quality grapes in the Barossa to actually source from. You cannot just make more fantastic wine (AU03).*

*In the top wines, it is definitely about the product (...). There are no accountants involved in any decision about wine (AU08).*

*The product first, obviously. We have always come out with products and then the demand followed that (CA10).*

In contrast to the Neoclassical Model the wineries tend to be utility-oriented and product-driven. Even though some winemakers admitted that they have to sell their wine in order to be able to keep on producing wine, all winemakers agreed on the (premium) product coming first. The demand follows.

The market for ultra-premium wine seemed to be able to pay less attention to broader fashions and trends on the mass wine market due to their smaller production volume and value creation mechanisms.

### *Reputation*

*Totally, in every aspect. We deliver consistent quality. That consistency gives you reputation (...). I do a lot of travelling, dinners and tastings. That is me personally taking about the family history, the setup, how we make our wine and how we grow the*

*grapes (...). There is a lot of stuff that we can do and do to influence our reputation (AU02).*

The winemakers were aware of their ability to influence the reputation of their brand.

*If you have a good product in the bottle, then after this point it is all about influencing reputation and preconception. Then you can drive the price up and everything is good (...). Rarity is a big thing. You have to be careful not to make too much of your best wine- even if you can (AU08).*

The producers seem to influence their reputation vigorously. Again, it begins with a consistent production of high-quality, which they communicate actively. They operate tasting rooms, hold wine dinners, host tastings at wine stores and portrait their winery closely linked to their core values, which indicate quality. Intangible factors as uniqueness, authenticity and experience play an important role in defining the premium qualities of a brand (Allsopp, 2005, p.189).

## 5. CONCLUSION

The study proved that institutions and mechanisms of reputation influence the value creating process on the premium Australian and Californian wine market. Finally, a strong interdependency of quality, price, and reputation showed that institutions, like wine experts, wineshows, and wine producers influence the quality perception on the market significantly and, thereby, reduce uncertainty to create the basis for market transactions.

Quality is described by intrinsic and extrinsic quality dimensions and consists of objective, relative and subjective quality factors.

The winemakers` understanding of quality is closely linked to the quality of the vineyard and the fruit. High vineyard quality, as low-yielding (old) vines, that produce small, thick-skinned, concentrated grapes, indicates high-quality wine with subjective and intrinsic quality characteristics as balance, complexity, structure, and personality. Continuously high-quality perception leads to a high individual reputation, which legitimizes high prices which in turn correlate with high-quality expectations and, thereby, create a quality equilibrium.

The further hypotheses were corroborated, as winemakers proved to influence the quality creating process, by also defining quality on the market, and by portraying their winery actively. While avoiding commercial motives, values as tradition, history, and a strong quality focus underline the authenticity of the premium brands. Winemakers communicate these values on the market, e.g. in wine dinners, wine tastings, and their tasting rooms, and, thereby, define quality and act as institutions of value creation.

As reputation effects are larger than effects of current quality, the winemakers profile by establishing quality indicators related to their wine the distinctive value of their brand.

The only observed significant difference between the Australian and Californian wineries is the average opinion about the closure of the wine bottle, while mostly agreeing on the fact that a natural cork closure generally indicates quality on certain markets. While for most Australian winemakers the lack of reliability is the main reason for avoiding natural cork, the Californian winemakers seem to have had much lower rates of cork failure experiences in recent years. Thereby, the main motives for the use of natural cork in California are tradition, sustainability in connection with the fact that wine is a natural product, which needs the cork closure for proper aging.

Finally, it must be stated that the results of this study are consistent with the current state of research. Wine quality consists from the producers' perspective as well as from the consumers' perspective of objective, relative, and subjective factors. Quality measurement is mostly about quality experience.

As institutions indicate quality and reduce uncertainty on the market, this paper reveals the major influence of the producers for the perception of quality on the premium wine market.

It would be of utmost interest to evaluate in further studies the effect of new media channels on the quality equilibrium, due to the growing independence of consumers in forums and blogs as new institutions.

## 6. ABOUT THE AUTHOR

Thomas Werdelmann is a Consultant at the Premier Management and Marketing Group (PMG) in Munich and a Ph.D. student of the University of Trier. In his previous research he focused on experience goods and market analysis of the music, art, and wine market. He holds a MBA degree from the University of Applied Sciences in Kempten and a Diploma in Educational Science of the University of Federal Armed Forces in Munich. As part of his MBA studies he spent 6 months at the Queensland University of Technology in Brisbane and 6 months at the University of California in San Diego to conclude his Master Thesis and concentrate on his research on the wine market in a close relationship with the Californian and Australian top wine producers.

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