Network governance in marketing channels

An application to the French Rhône Valley AOC wines industry

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Abstract

Purpose – This paper sets out to investigate the view that a firm's strategy in a marketing channel is contingent on the organization of its related upstream network of embeddedness.

Design/methodology/approach – An in-depth documentary study of recent developments in marketing channels in the French Rhône Valley Appellation d'Origine Controlée wine industry combined with content analysis of qualitative data derived from interviews with local wine merchants and Inter-Rhône wine experts.

Findings – The extended theoretical framework used in this case study enables researchers to more completely specify channel members' behavior. By taking into account not only general objectives but also legitimacy concerns of this type of organizations, it is possible to identify reputation and institutional commitment management in the upstream network as two governance mechanisms of equal importance to the mechanisms of vertical integration or management of relationships with suppliers.

Research limitations/implications – This study suggests the need for further research into external validity and measurement issues.

Practical implications – The study highlights the necessary governance mechanisms wine merchants have to deploy in their upper professional and supply networks in order to enhance their market performance. Successful positioning strategies seem to be more and more dependent on the wine merchants' ability to acquire a strong position and recognition in its upstream networks: only those who have taken into account the legitimacy issue and have deployed mechanisms to govern it effectively will survive the current internationalisation processes and avoid market decline.

Originality/value – This more nuanced channel approach offers a number of empirical illustrations to support the tri-dimensional conceptualization of institutional environment suggested by Grewal and Ravi in 2002.

Keywords Distribution channels and markets, Buyer-seller relationships, Wines, France

Paper type Research paper

This paper examines how a firm's strategy in a marketing channel is contingent on the organization of its related upstream network of embeddedness. On the basis of recent research carried out beyond the classical political economy theoretical framework into institutional influences and emerging networks, the author argues that a firm's ability in a marketing channel to adapt to downstream customer relationship changes depends on the governance mechanisms that have been deployed in its upstream network. These mechanisms are driven by two types of strategic goals:

The empirical work for this study was conducted as part of the PRATIC Research Team programme, in partnership with the Intra-trade Association: Inter-Rhône.

British Food Journal
Vol. 108 No. 4, 2006
pp. 256-272

0007-070X
DOI 10.1108/00070700610657092

(1) To strengthen legitimacy.
(2) To reduce environment uncertainty and resource dependence.

A study of recent developments in marketing channels in the French AOC (Appellation d'Origine Controlée) wine industry helps to identify and give an initial description of these mechanisms. The article concludes by highlighting some managerial implications of the study and laying out a research agenda.

The extended comprehensive framework of marketing channels

Due to the uncertainties inherent in a focal dyadic relationship, governance mechanisms are required to permit flexible adaptation to changing circumstances (Williamson, 1991). Moreover, as shown by Wathne and Heide (2004) in their extension of the Transaction Costs Analysis model, adaptation to uncertainty depends on how a connected relationship is organized.

In a broad sense, inter-firm governance is defined in terms of initiation, termination, and relationship maintenance processes. As recalled by Heide (1994):

> The term "governance" is a shorthand expression for the institutional framework in which contracts are initiated, negotiated, monitored, adapted and terminated.

Within this definition, the term "contract" is used in a very broad sense. Essentially, governance includes aspects of establishing and structuring exchange relationships as well as of monitoring and enforcement.

Theoretically, governance mechanisms in a supply chain network can correspond to two main strategic goals of the organizations involved:

(1) Reducing resource dependence and environment uncertainty.
(2) Strengthening legitimacy.

In the former case, the governance mechanisms will consist of either vertical integration or incentive design (i.e. participative decision-making and relational management of suppliers). In the latter case, they will take the form of the means of controlling a firm's image and reputation, mainly through ensuring the firm's embeddedness within the institutional environment.

Reducing resource dependence and environment uncertainty in marketing channels

Most research into marketing channels operates within a political economy framework, in which the channel dyad constitutes a social system influenced by economic and socio-political forces (Stern and Torger, 1980). Researchers have focused explicitly on internal economic and socio-political structures and processes, and the external economic environment (Achrol *et al.*, 1983).

More precisely, internal economy researchers have examined economic structures. Set within the transaction cost economics framework (Rindfleisch and Heide, 1997), this research has found that asset specificity (e.g. Anderson and Coughlan, 1987), environmental uncertainty (e.g. John and Weitz, 1988), and economies of scale (e.g. Klein *et al.*, 1990) influence the level of vertical integration. Researchers examining economic processes (i.e. the nature of decision-making mechanisms used by channel constituents – Stern and Torger, 1980, pp. 55-56), have found that centralization, formalization, and participation influence the functioning of channel relationships (e.g. Dwyer and Oh, 1987; John, 1984).

Internal polity research (i.e. the nature of the power-dependence relationships between channel constituents – Stern and Torger, 1980, p. 57) studies have examined the socio-political structure as the possession, use, and effects of the power of one channel member over another (e.g. Anderson and Weitz, 1992; Frazier, 1983b), the implications of the nature of dependence on channel-member attitudes (e.g. Kumar *et al.*, 1995; Lusch and Brown, 1996), and the performance consequences of control mechanisms (e.g. Bello and Gilliland, 1997; Celly and Frazier, 1996).

Following John (1984), researchers analysing socio-political processes (i.e. the dominant channel sentiments) have concluded that conflict (e.g. Frazier and Rody, 1991), trust and commitment (e.g. Morgan and Hunt, 1994), and social norms (e.g. Heide and John, 1992) influence channel attitudes. Beyond the micro-dyadic issues, channel researchers have scrutinized also the implications of the external economic environment and of the institutional aspects of the external polity for dyadic structures and processes.

In emphasising "uncertainty" and "dependence reduction", researchers have simultaneously developed two separate fields of enquiry that mirror developments in organization theory (Aldrich, 1979; Pfeffer and Salancik, 1978). Researchers in the first field who consider the environment as an information source – which results in the problem of uncertainty about external conditions (Aldrich, 1979) – have concentrated on the impact of environmental heterogeneity and variability on channel structures and processes (e.g. Achrol and Stern, 1988; Dwyer and Welsh, 1985). Researchers in the second field, applying resource-dependence theory, consider the task environment a stock of resources and raise the issue of channel-member dependence on the environment for critical resources (Pfeffer and Salancik, 1978; see also Achrol and Stern, 1988; Dwyer and Oh, 1987).

Emerging complementary perspectives on inter-firm governance and networks in marketing channels

Some scholars have suggested that in order to understand fully the nature of inter-firm relationships in marketing channels, greater attention must be directed to the larger inter-firm networks (Anderson *et al.*, 1994; Iacobucci, 1996). Recently, Wathne and Heide (2004), on the basis of the governance literature, identified two governance mechanisms that a manufacturer can use to structure his relationship with the upstream supplier and by doing so improve his ability to adapt to market changes: supplier qualification and incentive design. As they point out, current theory has proposed several strategies or governance mechanisms for organizations to manage relationships with exchange partners. According to Eisenhardt (1985) and Heide (1994), the mechanisms generally fall into two categories: a firm can *ex ante* identify or select a partner firm that possesses the ability and motivation to support its strategy and/or can design incentive structures that reward desired behaviour patterns, and/or penalize non-compliance in an ongoing relationship with a partner.

Beyond taking into account upper-relationship influence, other researchers have extended the level of analysis to upper networks in which channel members are embedded. The institutional approach, unlike the political economy approach, focuses on the necessity of organizational legitimacy. Institutional environments refer to the processes of institutionalization and corresponding institutions and mechanisms of influence that pertain to legitimacy in a particular societal context – legitimacy being defined as "a generalized perception or assumption that the actions of an entity [channel member] are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (Suchman, 1995, p. 574).

In their research, Grewal and Ravi (2002) extend the political economy framework by developing three institutional processes (regulating, validating, and habitualizing) that lead to the formation of types of institutions (regulatory, normative, and cognitive, respectively). They suggest that the institutional processes result in institutional pressures, which in turn influence channel structures and processes. Benjamin and Poldony (1999), study of status, quality and social order in the California Wine Industry shows that if, according to economic models of reputation, customers' expectations about the quality of a producer's products derive from past experience of those products, they also derive from affiliations that market actors develop through their exchange relationship. The status-based model of market competition shows that a market actor's status has a dual foundation in both its past demonstrations of quality and the status of its exchange partners (Poldony, 1993). Drawing on that model, they claim that a firm's position in the status order influences the attention that others pay to quality, their assessment of quality, and their regard for the product more generally. Therefore, relative to lower-status firms, higher-status firms derive greater benefit from producing a product characterized by a given quality. In many cases, differences in reputation may not be ascribable solely to differences in the underlying capabilities of producers, but rather to differences in the pattern of affiliations – which is where the firm is located in the social structure of a market. The affiliations or associations formed by the firm can strongly influence the perceived quality of the firm within the market. Specifically, firms receive lower returns on their quality investment if they fail to establish affiliations that reflect that investment (Benjamin and Poldony, 1999, p. 21).

Research into partitioning processes offers another interesting insight into channel behaviour. For example, Swaminathan (2001) suggests a prominent role for an organizational form's identity in resource partitioning. Typically, mature industry is characterized by a high degree of market concentration. With increasing concentration, generalists tend to compete vigorously for the central part of the market, thus allowing specialists to thrive on the periphery. But Swaminathan's study shows that the success of generalist organizations in establishing robust identities (through brand proliferation coupled with higher advertising expenditures) will depress the founding rate and elevate the mortality rate of specialist organizations. He suggests that useful insights into industry development can be obtained by categorising mature industries into two strategic groups, generalists and specialists, the respective characteristics of which – small size and a reputation for high quality – play an important role in the evolution of specialist organizational form. A longitudinal study of Californian wineries demonstrates that those owning larger vineyards suffer less mortality, possibly due to their greater control over the quality of raw materials. Vineyards tend to have a monopoly of the best-quality grapes and thus disadvantage those farm wineries without vineyards, which necessarily depend upon external grape supplies.

There is also considerable debate about the role of communal support structures in the development of specialist organizations. Swaminathan, following Piore and Sabel (1984), argues that various forms of institutional cooperation help in the growth of specialized wine-making districts, as they did, for example, in the development of specialized textile manufacturing areas in Italy. Some institutions, such as trade associations, guilds and unions, serve a socio-political purpose, providing a collective voice for specialist firms within an industry. Others, such as purchasing and marketing cooperatives, fulfil an economic rationale. Specialist organizations in mature industries are likely to develop in harness with other forms of specialist organizations (Swaminathan, 2001).

Recent research would indicate that the political economy approach and the institutional approach are complementary and that a consideration of both allows us to better understand channel dynamics. When analysing strategic changes in a particular industry, a combination of these theoretical approaches (see Table I) would potentially allow channel members to more fully grasp the precise components of such change and by doing so would improve their ability to anticipate and manage developments in their industry.

As a first step towards demonstrating the validity of such an integration of theoretical approaches, we here apply them to an analysis of a marketing channel in a specific empirical context – the French wine merchant business.

Linking theory and practice: the French Rhone-Valley AOC wines channels

Our research focuses on the 43 Wine Merchants and Trading Organizations of the Rhône Valley area (RV) for two principal reasons. The French wine industry has some unique features that make it an especially compelling context for examining both the interaction between socio-political institutions and distributors and the legitimacy issue. Because the French wine industry is structured according to specific regions, we focused on the wine merchants of one such region – the Rhône Valley. A specific case study such as this is appropriate for a preliminary application of our theory as it permits a deeper analysis of the interactions of businesses within both the regional (Inter-Rhône) and national institutions and of the challenges posed by globalization on a regional level.

The largely exploratory research methodology employed relies partly on a documentary study of the wine industry and partly on a content analysis of qualitative

Channel members' organizational goals	Reducing resource dependence and environment uncertainty	Strengthening legitimacy
Main references used	Stern and Torger (1980), Wathne and Heide (2004)	Grewal and Ravi (2002), Benjamin and Poldony (1999)
Unit of analysis	Channel Dyad	Upstream network in which the channel member is embedded
Research focus	Dyad economic structure and processes. Dyad sociopolitical structure implications of the external economic environment on the dyad	Institutions and institutional processes (regulation, validation and habituation) and the pressures they exert on channel members
Governance mechanisms used by channel members implemented in their upstream relationships or network of embeddedness	Vertical integration suppliers selection and relationship management	Reputation management Institutional commitment: Regulation governance Validation governance Habituation governance

Table I.
Combination of two main research streams in marketing channels

data derived from half-structured interviews with 20 wine merchants and three in-depth discussions with the Inter-Rhône experts responsible for wine merchant issues. After presenting the research context (A), we analyse recent strategic changes in the industry (B). Third, we show that the application of the extended theoretical frameworks highlights the channel members' rationality and, further, allows a first specification of the hypothetical governance mechanisms that they tend to implement or maintain in their network (C).

A. Research context

The empirical context for our study is the French AOC wine industry. According to the OIV Ll'Office International de la Vigne et du Vin), the French share of the global wine market fell by 6 per cent between 1990 and 2001 against a background in which the relative share of exports in the international wine trade increased from 18 per cent in 1990 to 31 per cent in 2001.

The decline in the French share of the international wine market is mainly the result of competition from "New World" wine producers (Australia, the USA, Chile, Argentina and South Africa) committed to true marketing strategies oriented towards a global coverage of markets, professionals and consumers. New World producers have defined a clear positioning for their products and ranges, even at a national level. Their wines are original, because of their "terroirs", but also because of the very user-friendly and easy-to-understand design of the products. This results in a homogeneous marketing mix: wines and packaging of a new type (e.g. fruity wines aimed to satisfy the taste of the average consumer rather than that of "experts", and wines made out of single grape varieties that are marketed with amusing or artistic labels); complete ranges of wines with easily identifiable brands (e.g. Gallo's "Turning Leaf"); pricing policies in line with the different quality levels; and well conceived advertising campaigns upon which no expense is spared. In addition, these producers have recently started to upgrade their ranges so that whereas they initially competed with lower-quality French table wines and "Vins de Pays", they are now also competing with higher-quality "AOC" wines (a total of 466 wines, from 112,000 wineries, that represent 80 per cent of total French wine production) which form the core of the French range.

The Rhône Valley, comprising 77,000 ha of AOC wines, is the second largest French wine producing area behind Bordeaux (117,000 ha), and one of the world's largest high quality wine producing regions. It is also a first class tourist area, so RV AOC wines function as the flagship for leading wine producers. In 2001-2002, 480 million bottles of RV AOC were sold. RV production, valued at 1.3 billion €, also represents 16 per cent of total French AOC wine exports in volume and 20 per cent of official French quality-wine production. In 2002, 28 per cent of RV production, valued at 30 million euros, was dispatched to over 150 countries, mainly in Europe.

RV AOC wines are produced and marketed by 1,529 private producers, 113 cooperatives, 43 wine traders and six cooperative groups. Local wine merchants bottle 50 per cent of the volume produced (representing 233 million bottles in 2003) and wine merchants from outside the area bottle 24 per cent, direct sales by producers representing 24 per cent of the total volume. Classified according to production regulation criteria, AOC wines can be summarized as follows (Figure 1).

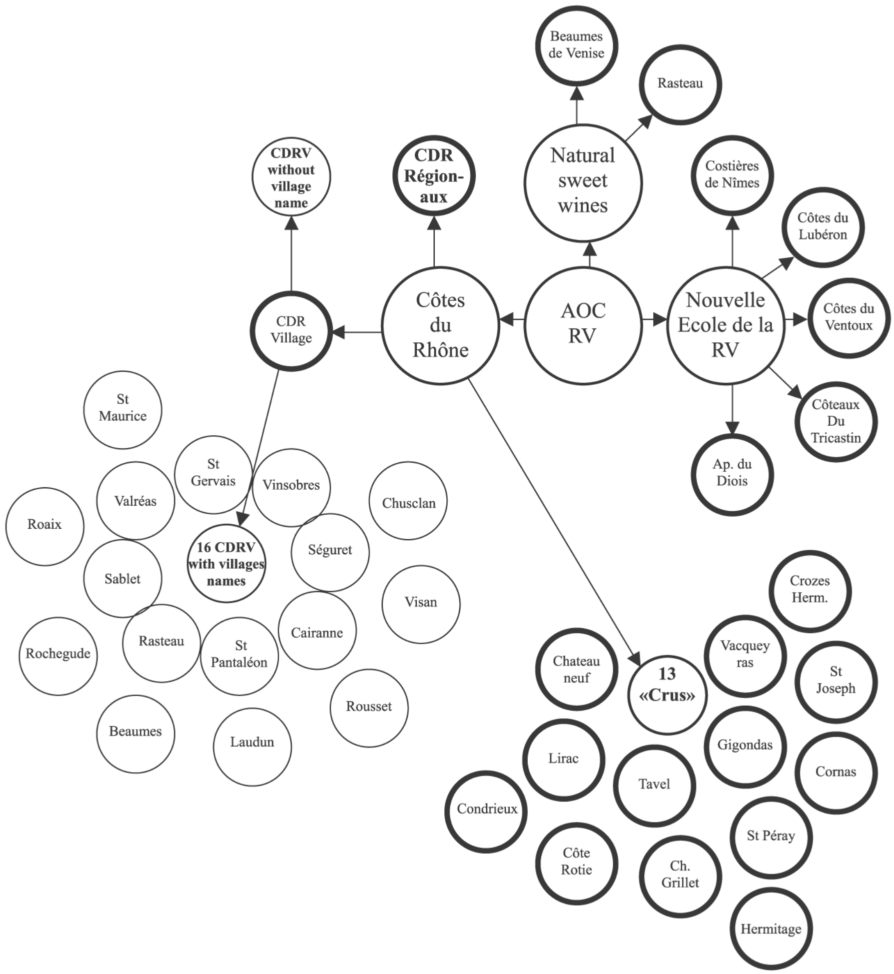

Figure 1.
The Rhône Valley AOCs

The 22 "statutory" AOCs have been classified by the Inter-Trade for historical and strategic reasons into three groups: Natural Sweet Wines, "Nouvelle Ecole", and Côtes du Rhone (CDR). The CDR category, which is more complex than the other two groups categorizes its wines according to the four AOC quality levels. They comprise 13 "Crus", officially the highest quality, followed by 16 officially allocated "village" wines, generic "CDR Villages" and finally CDR AOC wines.

B. Recent significant strategic changes in the RV wine merchants industry

Recent strategic groups movements

According to a classical Porterian strategic analysis, two criteria seem to structure the French AOC Wine Channels Industry: the percentage exported, and the percentage of sales in France outside the big retail stores. Five to six strategic groups were identified in 2003 against three in 1999 (Figure 2).

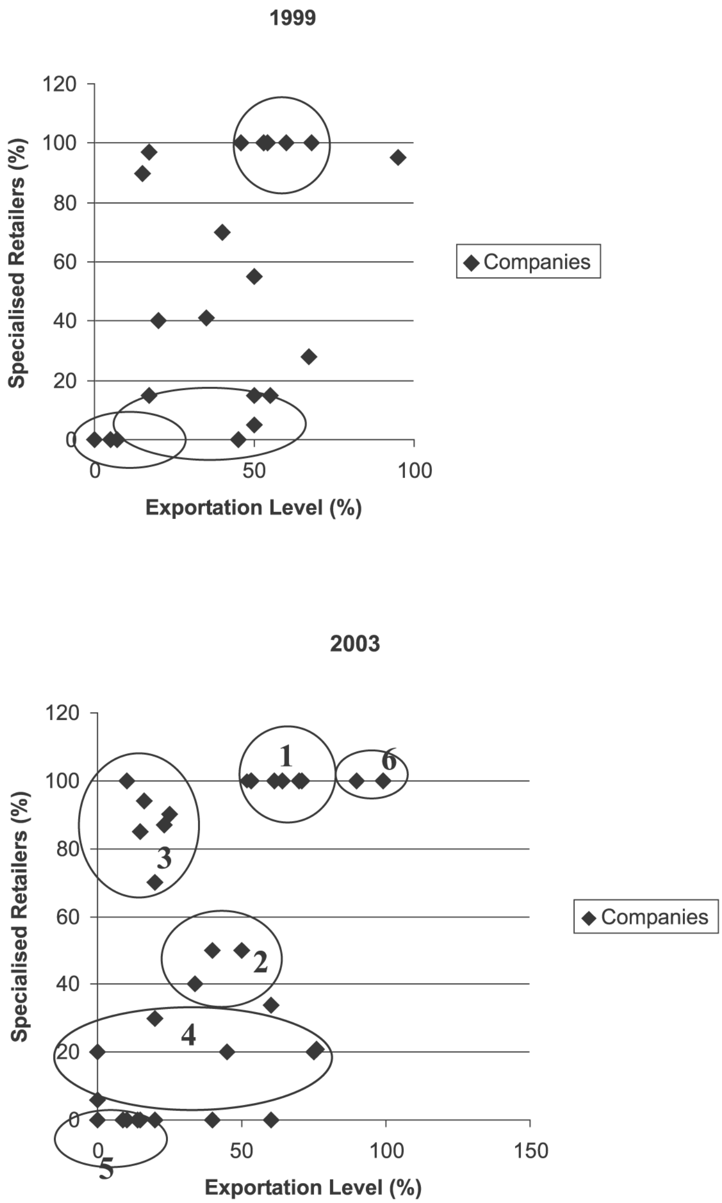

Figure 2.
The development of strategic groups in RV AOC wine marketing channels in 1999 and 2003

Ambassadors: 100,000 hl, 94 per cent RV AOC wines. This group consisted of:

- Four wine merchants who target high quality wine markets that are less sensitive to price (e.g. tasting and art segments).
- Family-owned companies – except one that, despite having been bought by Deutz Champagne ten years ago, has remained quite autonomous.

- Selective distributors who try to avoid major retailers and who sue specialized retailers who, by selling to major retailers, fail to respect their agreements.

Over the last five years, these companies have continued to expand spatially. For example, they currently tend to occupy all foreign markets for luxury goods and invest in high-quality vineyards, local and foreign. They follow luxury goods marketing strategies and maintain their positions on higher-quality expectations segments.

Challengers: 320,000 hl, 90 per cent RV AOC wines. This group consisted of:

- External investment and control: the Challengers comprise four companies, three of which have recently been purchased by large concerns outside the region, and one that was – with Australian financial assistance – purchased by its employees.
- Investment in local vineyards.
- A redesign of marketing strategies through brand or signature development and more generally an attempt to move away from the lower- and medium-quality towards upper-quality segments.
- An increase in buying safety through developing relations with winemakers and an enhanced selection of suppliers.

The Challenger group emerged during the last five years following investment by large companies external to the region. They tend to move into higher-value market segments.

Wine producers or "domains": 50,000 hl, 63 per cent AOC. Even though the volume and value of the AOC trade are about one quarter of those of the Ambassadors, the wine producers group has grown over the period 1999–2003. It comprises eight domains with relatively high levels of production and with such a good market performance that they are able to improve their ranges. For them, the wine trade is considered complementary to production, as a service – primarily for current clients – designed to achieve a better sales performance for the domain's existing ranges of wines.

Major retail suppliers: 1,300,000 hl. This group of eight companies faces increasingly fierce market competition, notably from cooperatives which have recently developed their own marketing processes, sometimes in alliance with other cooperatives and a set of clients (major retail stores) that are seeking to bypass wine merchants and establish direct relationships with producers.

"*Volumists*". These companies, which follow "volume" as opposed to "differentiation" strategies, can be divided into two groups comprising six bulk traders and four wineries. Volumists, like the "basic" market segment (people who drink wine at every meal), are in decline because they are being squeezed out by more efficient competitors.

"*Confidentials*". The sixth and final group comprises three wine merchants producing a total of 15,000 hl of top quality wines that are marketed in France and abroad.

Marketing development and repositioning of channel members

This study shows that there has been a complete repositioning of channel members in the French wine industry. At the regional level, new strategic groups are appearing in the upper-quality segments while groups in the lower-quality segments are fighting either to survive or to move up into the higher-quality sector. These strategic moves are in response to a market segmentation (Table II), based on a qualitative study of over 100 countries, presented to the local network by the regional Inter-trade organization.

Four segments can be distinguished:

(1) The "Food" segment should logically demand regularity, a safe buy, consistency, easy-to-handle packaging, wide distribution and reasonable prices.

(2) The "Fun" segment should correspond to standard wines. It is the "Soda" model of consumer habits. What is of value for the consumer is a universal, durable and recognizable taste, and the ability to find it easily in a crowded supply context.

(3) The "Tasting" group covers people who look for something special, specific or a different taste – as characterized by "terroir" and origins.

(4) The "Art" segment looks for an exceptional or unique sensation.

By overlapping strategic groups with recent international market segmentation (as shown in Table II), the coherence of positioning strategies becomes clear. By their very nature, strategic groups strive to progressively improve their adaptation to market segments (Figure 3).

Through the wine trade, "wine producers" are extending their product ranges. It is evident that the Challengers are producing two broad categories, one range with brand names designed for the major retailers, and another for the "Taste" and "Art" segments that imitates and is aimed to undermine the Ambassador range. Volumists are becoming more concentrated, while suppliers of the major retailers are trying to rebalance their portfolios and reduce their dependence on Major Retailers through strategies of internationalization. At the lower end of the fun segment and in the food segment, channel members are subject to the pressure both of direct sales by cooperatives (whether or not in alliance) and of direct purchases by major retailers who have already bought 2 per cent of channel members and who are also improving quality and moving up to the fun and tasting segments.

C. Understanding the channel dynamics through the extended theoretical framework

Through integrating the two main theoretical approaches of marketing channels, we argue that in the case of marketing channels for goods with strong identities in mature markets, such as the French wine marketing channels, the market adaptability of a marketing channel organization largely depends on its ability to manage its relations with the "upstream network" in which it is embedded (Granovetter, 1985). More

Price in Euros	Type of segment	Consumer expectations	Percent of world-wide demand	Trends
1-3	Food	Food complement	21	Decrease
3-7	Fun	Seeking standards and enjoyment	56	N/A
7-20	Tasting	Seeking special tastes, particularities	18	Increase
>20	Art	Seeking an emotion	5	Stable

Table II.
International segmentation based on consumer expectations

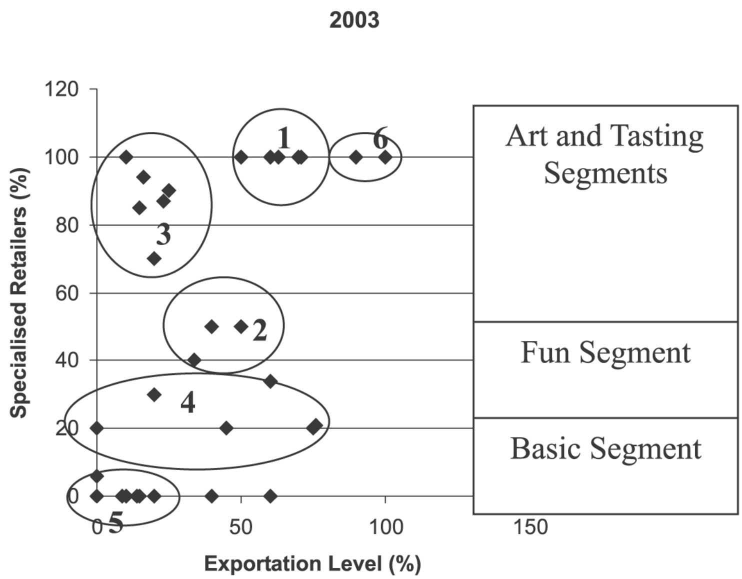

Figure 3.
Market segment adjustment of wine merchants marketing strategies in 2003

precisely, the governance mechanisms that this organization has deployed in its network will greatly influence its strategic ability to adapt to market changes.

Environment uncertainty, dependence reduction and corresponding governance mechanisms

The market adaptation of channel members presented above is closely linked to their ability to reduce uncertainty and dependence in their relationships with the production network. In a context of poor French wines sales on foreign markets due to sustained and aggressive competition from New World countries and a decrease in domestic demand, there is an increasing need for French wine merchants, who are responsible for 75 per cent of AOC wine sales, to adopt product quality management and precise positioning strategies. Wine merchants needing to maintain or improve their control on the supply network can utilize two main governance mechanisms: vertical integration and relational supply management.

Vertical integration. Vertical integration is one of the most effective governance mechanisms. Lately, Ambassadors have made huge investments in high-quality vineyards in the RV area and abroad: Guigal the leader of this strategic group has purchased Gripa Saint Joseph, one of the top ten vineyards of this specific AOC, while Chapoutier recently bought vineyards in Australia.

Challengers, following the example of Ambassadors, have recently expanded from the marketing to the production of prestige wines in order to control the top of their ranges and, whenever possible, they buy prestigious vineyards and domains. It is striking that, while five years ago all Challenger group companies were independent, all but two of them have now been bought by large French wine trade groups from outside the area: Boisset, Jean-Jean, Picard, and Skalli. In the major retailing suppliers group also, three members have been bought by large groups.

This vertical integration has recently been reinforced by the creation of Rhône Originals, launched in January 2005 as the result of an alliance between five local wine merchants: Ferraton Père and Fils, Meffre, Chapoutier, Grandes Serres and du Peloux. Its mission is to coordinate and strengthen the promotion of RV AOC wines on foreign markets – actions that will indubitably improve member control over the supply network.

Suppliers' selection and relationship management. More stringent selection criteria and better relationship management are the other governance mechanisms being developed by wine merchants in order to increase control over the AOC suppliers and to secure better relationships with the AOC Suppliers' network. In response to higher market expectations of quality, wine trade strategy currently concentrates less on pricing than on quality and product and wine merchants tend to implement, develop and maintain long-term relationships with strategic winemakers.

Indeed, in all strategic groups, relational mechanisms are being implemented towards the upper network. Channel members are rationalizing their supplier portfolios and developing ongoing cooperative relationships with selected winemakers. For example, they provide advisory services, such as regular oenologist visits. They also encourage winemakers who invest in quality and, in contrast to their prior tendency to abandon wine producers in poor years, provide sustained assistance to help them to complete their projects. In return, they expect the supplier to be transparent, refrain from cheating (for example by mixing good grapes with lower-quality grapes from untended plots), and to demonstrate loyalty to the Channel.

Commitment and trust in buyer-seller relationships are increasingly expected, while locally the prospect of economic difficulties has strengthened previously loose ties between network members. Decision making is becoming more participative, and wine merchants are increasingly expanding into wine making. More than ever before, Rhône Valley wine merchants are managing the risk of losing suppliers by creating interdependences that will sustain the quality of supply.

Legitimacy strengthening and corresponding governance mechanisms

The market adaptation of channel members is also linked to their legitimacy, defined by Suchman (1995), p. 574) as "a generalized perception or assumption that the actions of an entity [channel member] are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions". Legitimacy is a concept closely linked to issues of status and identity, which, as shown previously, respectively amplify quality perceptions and reduce activity risks. The more legitimate a wine merchant is perceived to be in the network, the more able he will be to influence network orientations and adapt to market fluctuations. In this context, two main interdependent governance mechanisms can be identified: reputation management and institutional commitment.

Reputation management. Wine merchants consider reputation to be a real asset because all their actions are measured in terms of their impact on company reputation and image. For example, some Ambassadors withdrew from the Russian market because of their inability to work within it in what they considered to be an ethical way. One Ambassador is suing specialized retailers who are secretly selling his wines to major retailers thus creating conflicts within the full network of specialized retailers and damaging the luxury image of company wines. Leading Ambassadors are also involved in "ethical" activities such as providing bottle labels in Braille for the blind or, whenever possible, biodynamic processes of production. They also sometimes participate in high-profile sponsoring of selected charities.

Nevertheless, the key issue as regards "reputation" focuses on the shared values that lie at the heart of French winemakers' "culture". Chief among these is quality. Thus all actions designed to improve quality are linked to both economic gain and socio-professional recognition. A wine merchant producing super-premium or "icon" wines that enjoy an international reputation is likely to be respected by all network members and thus be highly influential.

Institutional commitment. The second governance mechanism deployed by wine merchants to initiate, develop and/or maintain their legitimacy pertains to their behavior in institutional affiliations. Drawing on the Grewal and Dharwadkar (2002) framework of institutional environmental influences and more specifically on the three processes they identify: regulation, validation and habituation, we can distinguish three dimensions of channel-member response to institutional pressure:

(1) *Regulation governance.* Regulating processes, governing the interactions between channel members and regulatory institutions, take two forms: imposition and inducement. Imposition relates to the coercive power exercised by regulative institutions when they perceive that channel-member activities are in conflict with the larger societal good. When this occurs, the societal response is to create an apparatus of institutional coercion to regulate the activities of the channel member/s concerned. One example of this is the recent legislation in France curbing the advertising of alcohol – legislation that the French wine merchants' lobby has successfully agitated to soften with respect to advertising wine.

    Inducement relates to the provision of incentives (or disincentives) for channel members to conform (or not) to the demands of the agency offering the inducement. Here, wine merchants play an important role in advising government through their participation in a variety of state organizations, such as INAO (L'Institut National des Appellations d'Origine), CNAOC (La Confédération Nationale des Appellations d'Origine Controlée) and ONIVINS (L'Office National Interprofessionnel des Vins). For example, in response to a French Senate study of the wine industry that was directed by a former wine merchant, the wine merchants produced "white papers" on the current situation and prospects of the wine industry at both regional and national levels.

(2) *Validation governance.* Processes of validation subsume the midrange processes involving interactions between normative institutions (such as trade associations and professional associations) and channel members, and establish standards for socially acceptable behaviour (Baum and Oliver, 1991; Meyer and Zucker, 1989). Institutions, such as professional associations, may emerge to promote the interests of their members or create accreditation standards for their profession.

    Over the last five years, Rhône Valley wine merchants have become increasingly involved in the activities of Inter-Rhône which, in consequence, has increased its influence over AOC wine production and trade. Wine merchants use Inter-Rhône to enhance communication and cooperation between AOC producers, as occurred with the recent wine trade agreements and ten-year AOC Côte du Rhône strategic development plan.

Inter-Rhône is based on participative functioning and structured discussion groups involving the diverse AOC associations (about 1,500 independent producer units) and the Wine Merchant section (41 companies) that are automatically represented in every AOC syndicate. Inter-Rhône enacts decisions concerning, for example, the annual level of collective reserves or the procedures of control for each AOC. In the group meetings marketing or quality problems are also transparently discussed.

In addition to professional institutions, some Ambassadors participate in non-profit making associations such as the "Slow Food" Association (so named because of their opposition to "fast food" marketing concepts). Through this type of cross-professional body, they potentially enhance their field of operations and "legitimacy" image.

(3) *Habituation governance.* Habitualizing refers to the invisible, base-level institutional processes in which actions that are repeated become cast into a particular pattern that then can be reproduced with minimal effort and is recognized by its performer as the standard pattern (Berger and Luckmann, 1967). Habitualizing institutions emerge for two primary reasons. First, the creation of social order requires the adoption of routines that can be easily reproduced – which in turn leads to habitualizing. Second, psychological economies that result from the organizational ability to manage repetitive situations also require habitualizing (Berger and Luckmann, 1967). Habitualizing makes it possible for channel constituents to develop informal psychological contracts that are based on common understandings and which decrease the need for channel members to articulate structures and processes explicitly and regularly (Zucker, 1983).

French AOC wine networks have a long history and carry a system of implicit codes that orient members' actions and which are invoked when problems appear, as occurred in the tacit and largely non-concerted boycott of certain AOC producer networks that were judged by the wine merchants to have "misbehaved". Two RV AOC networks in particular have been "dropped" by some of the most important wine merchants because of opportunistic behavior that prejudiced the position of those wine merchants in the export market.

In sum, governance mechanisms may be understood as the specification of a general governance strategy implemented by channel members in their upstream network. Fully aware that "no business is an island", these organizations design incentive structures the long-term benefits of which for the upstream network exceed any possible short-term benefits derived by bypassing them. However, in order to reap the benefits of incentive structures, channel members have to reduce the perceived expropriation risks endured in return by their network and match the "investment" or the contribution of the latter to their own marketing strategies. It seems that they achieve this equilibrium through vertical integration and/or relationship management as well as through reputation and institutional commitment management.

Conclusion

Compared to the conventional political economy approach to the analysis of marketing channels, the extended theoretical framework used in this case study enables researchers to more completely specify channel members' behaviour. It also offers greater insight into the hypothetical sources of their strategic ability to adapt to market changes.

By taking into account not only general objectives such as the reduction of uncertainty and resource dependency, but also legitimacy concerns of this type of organizations, it is possible to identify reputation and institutional commitment management in the upstream network as two governance mechanisms of equal importance to the mechanisms of vertical integration or management of relationships with suppliers.

This more nuanced channel approach that focuses on "regulation", "validation" and "habituation" governance of upstream networks by channel members, offers many empirical illustrations to support the tri-dimensional conceptualization of institutional environment suggested by Grewal and Ravi (2002).

This study also suggests the need for further research into external validity and measurement issues through, for example, raising questions such as "what role does 'culture' play in network management?", "are these governance mechanisms specific to a particular industry?", and "what is related to the product category?".

From a managerial point of view, the study points out the growing complexity of the wine merchants' role by highlighting the necessary governance mechanisms they have to deploy in their upper professional and supply networks in order to enhance their market performance. Successful positioning strategies through product, price, distribution and promotion seem to be more and more dependent on the wine merchants' ability to acquire a strong position and recognition in its upstream networks. It would appear that only those who have taken into account the legitimacy issue and have deployed mechanisms to govern it effectively will survive the current internationalization processes and avoid market decline. Thus this research illustrates that the very nature of wine merchants' core competencies shifts from tasks related to being a link in the supply chain toward effectively "governing" their network of embeddedness and, within this context, becoming a key pilot organization.

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Further reading

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