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From Relationship Asymmetry to Market:

Spatial and Organizational Dynamics in Beer Wholesaling

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Abstract

This research focuses on how spatial and organizational dynamics affect the inequality among intermediary organizations. I explain why in the brewing industry the number of intermediaries (i.e. wholesalers) declined, while their suppliers (i.e. brewers) proliferated in the past 30 years. By focusing on factors of organizational structure and competitive pressure, I examine their survival chances and the factors that contribute to the expansion and diversity of their portfolio. Results explicate conditions under which organizations act in seemingly counterintuitive ways, outline new concepts to explain their behavior, and highlight the institutional consequences on how the shifting social logic underlying market transactions feeds inequality among intermediary organizations.

Takeaways

- Changing industry conditions affect the potential payoff of various market strategies and the inequality among organizations.
- The potential of newness principle shows that certain new entrepreneurs can have better survival chances than industry incumbents.
- High productivity organizations have a higher likelihood of representing any craft labels, value-based considerations of organizational matching matter less.
- Representing controversial 'good renegade' producers decreases most wholesalers' portfolio diversity but in highly competitive environments, a minority of wholesalers gain diversity.

Category: Strategy, Economic sociology

Keywords: Market Entry, Competitive Pressure, Portfolio Diversity, Inter-industry Dynamics, Environment-Strategy Fit

Executive Summary

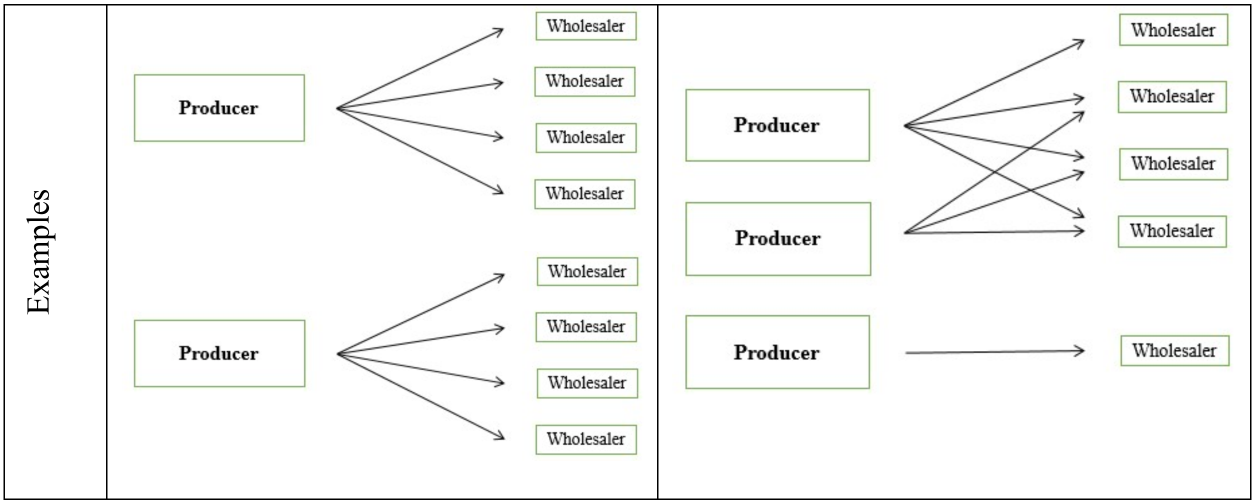
This dissertation investigates what happens with intermediary firms when the rules of the game underlying their competition change. Under these changing conditions, it is an open question which intermediaries keep up, get ahead at an accelerated rate or lose and leave the market. We have good theories that predict how firms in intermediary positions fare compared to firms who do not have this structural benefit. However, there is still room to investigate how specific groups of intermediaries fare in comparison to other intermediaries. In this research, I study boundary conditions of firms' strategic behavior regarding survival, portfolio expansion, and portfolio diversity. Results explicate conditions under which organizations act in seemingly counterintuitive ways, outline new concepts to explain their behavior, and highlight the institutional consequences on how the shifting social logic underlying market transactions feeds inequality among intermediary organizations.

I use the segment of beer wholesalers as a case to test the effects of dynamic environments on the inequality among intermediaries. The empirical paradox I explain is why in the past thirty years as the number of beer intermediaries (i.e. wholesalers) declined while the number of beer producers (i.e. brewers) increased. I bring forward the argument that the opposite trends in closely connected market segments reflect a change in the underlying social structure of the market relationships. This framework emphasizes that the social embeddedness underlying economic transactions can make or break markets.

The changing social embeddedness of producer – wholesaler relations refers to a process in which the nature of market ties changes from one-to-many to many-to-many (Table 1). I call this the mechanism of differential expectations, to shift the focus to the potential returns of producer – wholesaler contracts and how it changed over time. Before the 1980s, wholesalers were local representatives of brewers' interests, as only a handful of breweries were on the market. They were like family to the brewers; trust and loyalty characterized their exclusive relationship. This social baggage of market transactions already interferes with "efficient" market processes, but even more unexpected outcomes arise when this structure begins to change. Breweries that entered the market in increasing numbers after the 1980s were small-scale, craft beer producers. They had little to no resources to acquire many wholesaler contracts, which contributed to a shift in wholesaler strategy as well. Instead of acting as local representatives of national companies, they provided knowledge and resources to scale the products of small labels. The resulting market structure is one in which many producers match with many wholesalers, and diversified portfolios emerge. Not only were these new relationships less socially embedded, but they also broke down the old, exclusive relationships as well.

Table 1: Changing social embeddedness of market transactions

	Time dimension →	
Market	One-to-many Exclusive relationship	Many-to-many Diversified portfolios



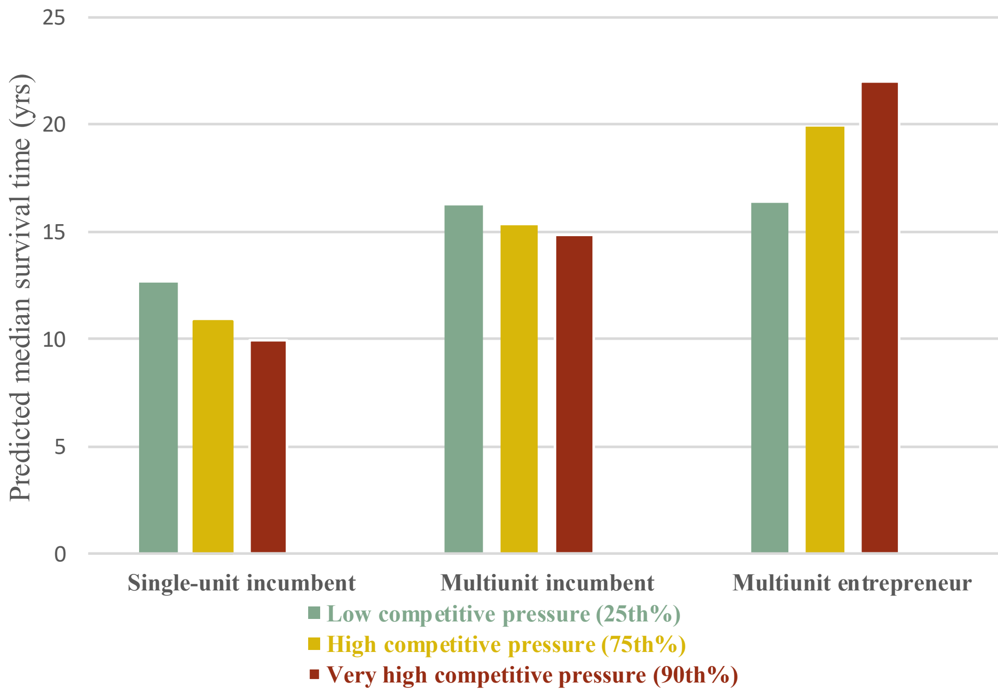
The consequences of the mechanism of differential expectations are the focus of the empirical studies. The paper entitled *Relationship Asymmetry and Potential of Newness: Historical Industry Dynamics of Entrepreneurship* compares the survival chances of intermediary market segment members. I use establishment-level restricted-access economic microdata from the Longitudinal Business Database between 1983-2014. Piecewise exponential models show that the mechanism of differential expectations affect intermediary entrepreneurs' survival chances in a way that is unexpected based on current theory. Results on the survival chances of entrepreneurs are consistent with Stinchcombe's liability of newness thesis as long as we do not account for firm structure: the hazards of market exit are higher for entrepreneurs compared to incumbents. However, once we distinguish between market entrants who are part of single-unit and multiunit firms, using organizational structure as a proxy for their resources, results explicate the boundary conditions under which Stinchcombe's liability of newness can get suspended. I find that multiunit new entrants have higher survival chances compared to both single-unit and multiunit incumbents. I call this effect the potential of newness, which highlights that there are market conditions under which newness can have bigger potential than predicted, based on current theory.

Moreover, I show that multiunit entrepreneurs disproportionately benefit from the potential of newness in highly competitive environments and where the industry experienced shakeouts. While these historical events lower the survival chances of incumbents, multiunit entrepreneurs experience an increase (Figure 1). I explain this counterintuitive effect using the mechanism of differential expectations: it is easier to create entirely new market ties than change old, socially embedded ones. Multiunit new entrants created diversified portfolios upon arrival while incumbents had to negotiate for the same change in their long-standing market ties. In many cases, incumbents found themselves trapped in contracts that no longer contributed to their organizational survival. These results highlight that market relationships are social and that a change in the underlying social logic of market relationships can have industry-changing consequences.

The results also highlight that there is a need to extend current research frameworks in entrepreneurship that allow studying the phenomenon among intermediaries (or 'non-producers') and in non-technology related fields as well. The resource-rich intermediaries do not represent our current thinking on who an entrepreneur is. While recent literature started to take into account the individual-level factors that an entrepreneur brings to the table upon starting a new venture, scholars paid less attention to the social capital and resources of businesses that switch industries. Some of the multiunit firms that were new to the beer wholesaling industry were already seasoned businesses in other industry segments. However, they needed to realign their resources and set up the technologies to be able to store beer in their warehouses. As such, they did entrepreneurial bricolage, but their available resources made them different from the entrepreneur described in the literature.

Figure 1: Historical conditions of the potential of newness.

Predicted median survival time (with 95% confidence intervals)



Source: Longitudinal Business Database. Estimates based on Model 3. All other variables are held at their mean. N=~80,000

In the paper entitled *Who takes on the Small Producers? The Spatial Structure of Competition,* I combine insights from economic and valuation-based theories to examine the factors of niche product representation and portfolio expansion. Building on the premise that different theories might have different explanatory potential on different levels of analysis, I outline expectations based on how an economist, an economic sociologist, and an industry participant would argue. I use the empirical case of beer wholesaling and conduct two analyses using a proprietary dataset (1997-2016) that includes wholesaler establishments from three U.S. states. In the first-stage, I use logistic regressions examining the factors that affect the odds representing any craft labels, then run least squares regressions to explain portfolio fit.

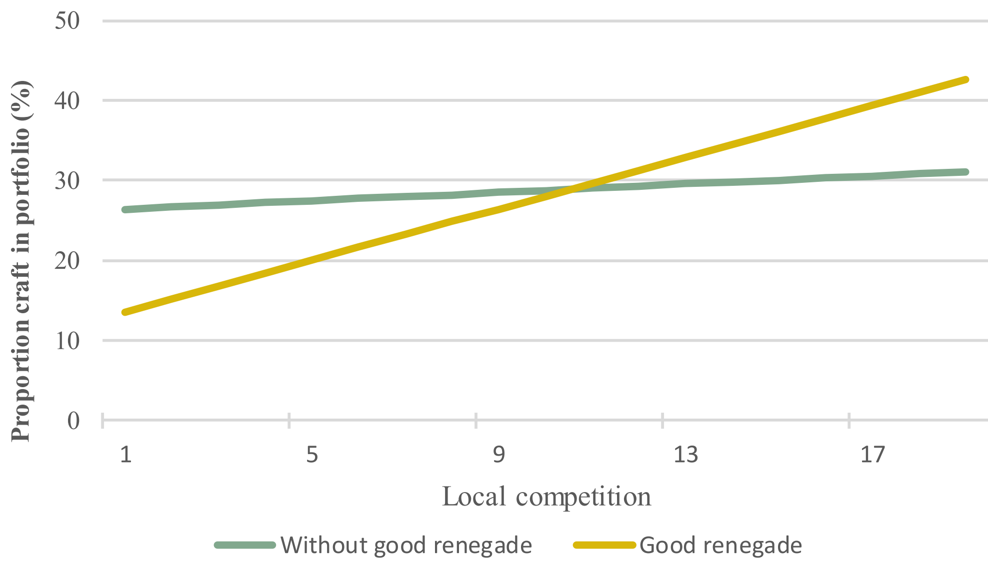
I find that high productivity organizations have a higher likelihood of representing any craft labels. This result goes against what industry participants believe and what we would expect if organizations worked with other organizations whose values they approve. It seems that because the transactions between craft breweries and large wholesalers remain hidden from the consumer's eye, breweries who are otherwise quick at dismissing big business practices, are using their services. Craft breweries partner up with large wholesalers who already represent big breweries in many cases.

Results also highlight that it is about how all the brands in a portfolio fit together, not whether a particular wholesaler already represents one of the big beer labels. A well-made portfolio contributes to both craft representation and portfolio diversity. This result suggests that intermediary firms should consider how a new market transaction affects the ones they already have in place, in each of their locations.

I find a further emergent portfolio dynamic: the importance of good renegade labels. These are initially small scale breweries who became controversial by growing too big for their category or get acquired by a large company. I find that if a portfolio represents a good renegade label, the portfolio does not diversify further, which hinders market access of latecomer craft labels. However, I find that this effect depends on where the wholesaler operates. While their overall effect is negative, good renegades facilitate portfolio diversity in highly competitive environments (Figure 2). High competitive pressure incentivizes fast organizational learning, and wholesalers can use the social networks of good renegades to find information about the quality of new brands. This association indicates that embedded relationships benefit only a few wholesalers and their producers. For them, business is going increasingly well, but this does not hold for everyone in the population.

Figure 2: The differential effect of good renegades on portfolio diversity

Predicted probabilities of portfolio diversity by conditions of local competition



N=724

My research proposes two generalizable concepts. They each highlight the context dependence of organizational behavior and contribute to the literature on organization theory and strategy. The potential of newness principle describes the capacity of organizations to strategically act upon industry conditions and leverage their positions to get ahead. This concept adds to the strategy literature on competitive advantage and dynamic capabilities. The concept of good renegades outlines a process in which firm evolution blurs the boundary between large producers and small-scale craft organizations. It contributes to theories on resource-partitioning and evolutionary perspectives of the firm.

The framework of this research allows us to think about how unequal embeddedness of market relationships can make or break organizations and contribute to organizational inequality. It highlights that market structure not only enables but sometimes traps already existing organizations and makes them less adaptive to changing industry conditions. We know that competition works to the benefit of the highest status organizations: frequently the rich get richer. But an industry-wide change in the underlying social structure of market transactions can make some groups get richer even quicker in highly competitive environments: resource-rich wholesalers who open new establishments and wholesalers who have good renegades in their portfolio.