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## **Entrepreneurial and Buyer-Driven Local Wine Supply Chains: Case Study of Acres of Land Winery in Kentucky**

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### **Abstract**

The Kentucky wine industry has grown rapidly over the past decade as farmers diversify from tobacco to alternative enterprises. The objectives of this paper are to; (i) describe the conversion of a family-owned tobacco farm into a fledgling wine enterprise (ii) identify market competitive and coordination strategies being used by an emerging winery, (iii) determine key challenges facing the development of a small winery and (iv) recommend future studies for improving the performance of local wine supply chains. The paper is based on a case study of Acres of Land winery in Kentucky and it uses qualitative data collected during visits to the farm in 2007, 2008 and 2009. The case study shows the development of the winery and the organization of the local wine supply chain. Results indicate that Acres of Land winery is fully vertically integrated and actively pursues both competitive and risk management strategies. The winery faces challenges such as “dry county” restrictions, government licensing requirements, changing consumer preferences, and growing industry competition.

**Keywords:** local, winery, marketing, promotion, strategy, Kentucky

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## Introduction

Kentucky’s wine industry has grown rapidly over the past decade despite the difficulties of creating a reputation for high-quality products facing most new wine growing areas (Loureiro 2003). The compensation of producers from the federal tobacco buy-out program coupled with the entrepreneurial ingenuity of the local farmers has contributed to a resurgence of wine production as a statewide diversification strategy. The US tobacco “buyout program” also known as Tobacco Transition Payment Program (TTAP) was designed to ease the transition for US tobacco quota holders and producers from the Depression-era tobacco quota program to the free market (Pushkarskya and Marshall 2009). After the signing of the Fair Equitable Tobacco Reform Act of 2004, annual transitional payments for up to 10 years were made to eligible tobacco quota holders and producers with the funding coming from the \$10 billion assessed on tobacco product manufacturers and importers. The end of the tobacco quota program prompted farmers to exit tobacco and pursue alternative crop enterprises (Beach et al. 2008).

In Kentucky, the emergence of entrepreneurial small wineries is part of ongoing initiatives to diversify the agricultural sector from tobacco to alternative crop and livestock income-earning opportunities. Wine production has become one of the key enterprises that are expected to grow in the future (Futamura 2007). The Kentucky Department of Agriculture (KDA) has established a website, Kentucky MarketMaker™ to provide market information to potential customers and visitors and help them locate the 60 wineries that are currently in operation in the state. Historically, wine marketing has been dominated by the “Old World,” comprising Western European countries: France, Italy, Spain and Germany (Jordan et al. 2007). Recent growth in global market penetration of wines from the so called “New World,” comprising US, Argentina, Australia, South Africa, and Chile, has reconfigured the marketplace making the industry highly competitive (Hussain<sup>a</sup> et al. 2007). The emergence of Brazil as a key global player in wine production (currently ranked third in South America behind Argentina and Chile, and 17th globally) has further intensified the already fierce competition (Fernsterseifer 2007). In the US, relatively new players from non-traditional wine producing states have entered the market leading to a significant growth in the number of small wineries in operation. Several states have experienced an emerging winery industry including Colorado, Kentucky, New Jersey, North Carolina, and West Virginia (Phillips et al. 2009; Maumbe 2012). However, California still produces 88.6% of all of the wine in the US and the top ten wine-producing states cover 98.5% of the market (see Table 1) (Dept. of Treasury 2012). Increasing production and consumption of wine from non-traditional wine producing states is also part of the rising consumer interest in buying locally grown agricultural products. The US Department of Agriculture’s Agricultural

**Table 1.** Top Ten Wine Producing States in the US

State	Percentage of total production	State	Percentage of total production
1. California	88.6	6. Kentucky	0.3
2. New York	3.7	7. Florida	0.3
3. Washington	3.6	8. Ohio	0.2
4. Oregon	0.8	9. Michigan	0.2
5. Vermont	0.5	10. New Jersey	0.2

**Source:** Dept. of the Treasury, Alcohol and Tobacco Tax and Trade Bureau. 2011.

Marketing Service has been recording double digit growth in farmers markets over the last decade and major food retailers have also established policies encouraging purchases from local farmers (Martinez et al. 2010; Thilmany McFadden and Low 2012).

The driving forces behind the recent growth in the US wine industry vary from state to state. Differences in state laws regarding production and distribution of wine, new economic opportunities, buy local campaigns, growing taste for wine among the millennial generation, environmental sustainability, product knowledge, and fair pricing relative to quality are some of the key factors influencing demand for wine and the development of small wineries in the US and abroad (Nowak et al. 2006; Hussain<sup>b</sup> et al. 2007; Alonso 2010). Small wineries in the US face growing economic challenges of providing quality, taste, safety, cost efficiencies, and variety. Enterprise competitiveness and environmental sustainability are of strategic importance to small winery operations (Barber et al. 2010). Despite these challenges, local wine supply chains (LWSC) are booming and wineries are providing alternative income sources for previous tobacco farmers in Kentucky. The rising buyer-power expressed in terms of low switching costs to competing brands, consumer demand for consistency, healthfulness, and environmental attributes have made private vertical coordination and strategic alliances an essential part of wine niche marketing. Eco-labels are being used to signal environmental attributes, reduce information asymmetry between producers and consumers, and enhance demand for wines perceived to be environmentally favorable (Delmas and Grant 2008). The future survival of small wineries will depend on better market coordination (i.e., procurement, post-harvest cold storage, transportation services, etc.) and access to market information for better decision making. Entrepreneurial approaches being used by winery operators that are contributing positively to their success include the ability to exploit new market opportunities, provision of innovative customer centric products, enterprise diversification, and risk management (Morrish et al. 2010).

Small wineries in the US have to cope with the challenges of changing consumer demand for product quality, health and safety, business risk, and the need for better market coordination and sustainability. A growing challenge facing the food industry generally is the judicious use of scarce environmental resources (Bena et al. 2010). The ability of small wineries to address such challenges is limited by their lack of economies of scale, relatively high transaction costs due to information asymmetries and asset specificity, and the low potential for investment capital in most of the emerging wineries. Yet consumers do not discriminate between highly capitalized large agribusiness firms and small wineries in their demands for high quality, safe, healthy, environmentally friendly, and consistent products.

Nonetheless, small wineries have to maneuver within their local supply chains and limited resource endowments to find solutions to these demands or risk losing market share to well-established global wine supply chains. For their long term survival, operators of small wineries have to be innovative and entrepreneurial in differentiating their products, developing niche markets, and adopting consumer-orientated supply chains committed to creating superior value for customers. The Australian wine industry success is partly attributed to a positive relationship between market orientation (i.e., customer and competitor orientation) and business performance (Jordan et al. 2007). Further, innovative value proposition arises from a creative and innovative opportunity-seeking marketing focus (Morrish et al. 2010). Managers of small wineries have to

grapple with several issues including how to; (i) minimize long-run operating costs and negative externalities that might damage their reputation, (ii) pursue focused differentiation in niche markets, and (iii) build trust-based partnerships and diversify income in order to absorb the shocks from unexpected business failure.

The specific objectives of this case study are to; (i) gain insight into how former tobacco farmers are managing the transition from a commodity-based operation to a customer-focused direct-marketing enterprise, (ii) identify market competitive and coordination strategies needed in a vertically linked local supply chain, and (iii) determine key challenges facing the development of small wineries. The rest of the paper is organized as follows; section 2 provides an overview of the history of wine production in Kentucky and historical development of Acres of Land Winery (AoLW). Section 3 describes the conceptual framework. Data collection is described in section 4. This is followed by results and discussion in section 5. Section 6 highlights key challenges confronting small wineries in the US, and section 7 concludes the paper, including recommendations for future studies of local wine supply chains.

## **Establishment of Acres of Land Winery**

Kentucky was home to many of America's early wineries in the 1700s. The enactment of federal Prohibition Laws in 1920 prevented the manufacture, sale, and transportation of alcohol used for consumption. This marked a decline in vineyards in Kentucky and around the US and an expansion of tobacco production. Growing public health concerns and passage of the Net-Cost Tobacco Program Act in 1982, which shifted the burden for tobacco program losses from the federal government to growers, resulted in a decline in tobacco production as local producers sought alternative sources of income (Woods 1998). (For an overview of the history of wine production in Kentucky see Appendix 1).

As shown in Table 2, AoLW embarked on alternative production activities in 1998. The family farm, which is 400 acres in size with 12 full-time and 8 part-time employees, had been in existence for over 50 years with burley tobacco as its main enterprise. It is located in Madison County, a little over 30 miles from Kentucky's second-largest city, Lexington, home to the University of Kentucky. The decline of AoLW's burley tobacco quota triggered diversification into an agri-tourism (agri-tainment) business that later became AoLW. The first grapes were planted in 2000; grape varieties currently grown are *chambourcin*, *vignoles vinerifa*, *carbernet*, *reliance*, *mars*, *sauvignon* and *chardonnay*. These grapes are used to make a wide variety of wines that are produced and marketed under the AoLW brand. In 2003, AoLW developed a wine producing and bottling facility with a capacity of 750 bottles per hour. A selection of AoLW wines is listed in Table 3. The wines are named after local people who owned parcels of land on the farm over the years. Online orders from the winery's wine list allow customers who are unable to visit the farm to purchase wines in their local stores. In addition, AoLW has a restaurant on site that serves not only its wine but other products produced on AoLW land and neighboring farms. As shown in Table 4, AoLW has earned brand recognition from the numerous awards it has won at major regional and international wine competitions. The main vision behind AoLW's effort to raise market awareness is the need to advance the goal of *saving family farms and communities* in Kentucky. Most consumers find the notion of protecting American farms a cause they can identify with, thus creating the opportunity to convert prospects into customers.

**Table 2.** Historical Development of Acres of Land Winery, 1998-2010

Year	Key Production and Marketing Developments
	AoLW was a typical tobacco farming operation doing business for more than 50 years prior to the winery
1998	Diversification into wine production started.
2000	First vineyards planted on 1½ acres of land.
2003	Wine production facility established.
2004	Commercial wine sales started in December
2005	A full service 150 seating capacity restaurant with gift shop and wine tasting room established.
2007	Wagon rides through vineyards added to tours of winery building and picnic locations.
2009	Winery full-service restaurant gutted by fire on March 21 <sup>st</sup> .
2010	Rebuilding starts on new Acres of Land Winery restaurant.
2010	New restaurant opened to customers in October.

**Table 3.** List of Wines Produced by Acres of Land Winery, 2010

1. Kentucky Chardonnay	10. Kentucky Chambourcin
2. A.I. Vidal Blanc	11. Concord
3. Chenin Blanc/ Viognier	12. Willie Mae’s Blackberry
4. Vignoles	
5. Maggie Adams Blush	
6. Colonel’s Ridge Cabernet Sauvignon	
7. Phoenix	
8. Marie’s Merlot	
9. Russell Land Reserve Chambourcin	

**Table 4.** Acres of Land Winery Awards, 2005-2010

Name of Wine	Award	Year of Competition and Description
Kentucky Chardonnay	Silver Medal	2007 Taster’s Guild International Wine Judging
Kentucky Chardonnay	Bronze Medal	2007 Northern Kentucky Wine Festival
Kentucky Chardonnay	Bronze Medal	2006 Taster’s Guild Wine Lover’s Competition
A.I. Vidal Blanc	Silver Medal	2007 Taster’s Guild International Wine Judging
A.I. Vidal Blanc	Bronze Medal	2006 Taster’s Guild Wine Lover’s Competition
A.I. Vidal Blanc	Silver Medal	2005 Taster’s Guild International Wine Judging
Vignoles	Bronze Medal	2007 Taster’s Guild International Wine Judging
Vignoles	Bronze Medal	2007 International Eastern Wine Competition
Vignoles	Bronze Medal	2006 Taster’s Guild Wine Lover’s Competition
Maggie Adams Blush	Bronze Medal	2007 Northern Kentucky Wine Festival
Maggie Adams Blush	Bronze Medal	2006 Taster’s Guild Wine Lover’s Competition
Maggie Adams Blush	Bronze Medal	2005 Taster’s Guild International Wine Judging
Phoenix	Silver Medal	2010 Kentucky State Fair
Colonel Ridge’s Cabernet Sauvignon	Bronze Medal	2006 Taster’s Guild Wine Lover’s Competition
Colonel Ridge’s Cabernet Sauvignon	Silver Medal	2005 Taster’s Guild International Wine Judging
Marie’s Merlot	Bronze Medal	2007 Northern Kentucky Wine Festival
Marie’s Merlot	Bronze Medal	2005 Florida State Fair Wine and Grape Juice Competition
Russell Land Chambourcin Reserve	Gold Medal	2005 Taster’s Guild International Wine Judging
Kentucky Chambourcin	Bronze Medal	2005 Florida State Fair Wine and Grape Juice Competition
Concord	Bronze Medal	2006 Taster’s Guild Wine Lover’s Competition
Concord	Bronze Medal	2005 Florida State Fair Wine and Grape Juice Competition
Concord	Bronze Medal	2005 Taster’s Guild International Wine Judging
Willie Mae’s Blackberry	Bronze Medal	2006 Taster’s Guild Wine Lover’s Competition

## Conceptual Framework

The conceptual framework for this study draws upon agribusiness strategic management (i.e., industry driving forces, key success factors, and competitive advantages), supply chain management, and transactions costs theory. The internal and external factors driving the operations and competitiveness of the winery are considered in the context of supply chain management (SCM) theory (Gunasekaran et al. 2008). The SCM framework focuses on producer linkages with suppliers and customers to achieve integrated value chains using information technology. But high *transactions costs* in supply chains can lead to market failure and can hamper competitiveness (Hobbs 2003). Transaction costs which include *search costs*, *negotiation costs*, *monitoring* and *enforcement costs* result in different methods of organizing transactions from *spot markets* to *contracts* to *vertical integration* (Williamson 1979; Hobbs 2003). Drawing from strategic management theory, key internal and external forces confronting small wineries can be analyzed as *key industry success drivers*, *competitive strategies*, and *nature and sources of transactions costs* (see Figure 1). The combined negative influence of industry forces can hinder the ability of small wineries to gain sustainable competitive advantages. In contrast, effective market penetration and coordination strategies can result in competitive advantages and significant reductions in information asymmetry and transaction costs in LWSC.

Local supply chains have the advantage of geographic proximity for building trust-based relationships with supply chain partners and customers. Wineries maintain total control of the significantly shortened supply chain when they directly market their wine to consumers who are visiting the vineyard and winery. The product then takes on additional attributes related to the experience of meeting the winemaker and seeing the vineyard. Information asymmetries disappear when consumers can taste the wine and trust is built in the atmosphere of the wine tasting room or restaurant. Loyalty can develop when consumers see who is being supported by their purchase. But for small wineries to expand their markets they may need to go beyond marketing directly to agri-tourism customers. Focusing on local supply chain partners that will maintain place-based authenticity of the brand through tastings and support for a “buy local” campaign can be a useful strategy for small wineries whose main market is within their local region, especially if they are located near a metropolitan area.

### *Key Industry Success Drivers in Wine Marketing*

The marketing of wine is constantly evolving and mature wine markets such as France, Italy and Spain are threatened by wines from the “New World” (Terblanche et al. 2008; Hussain<sup>a</sup> et al. 2007). The forces of change affecting the wine industry are being felt at the global and local levels. These key wine industry driving forces are growing competition, over-production, changing tastes and preferences, decline in demand for wine relative to other beverages, health and safety issues, environmental consciousness of consumers, location, and land use issues (Terblanche et al. 2008; Baer et al. 2010; Alonso, 2010). Foster et al. (2002) argue that the key decision areas affecting the success of wine supply chains are: senior management involvement, plant and equipment, quality control and assurance, production planning and control, and product design. The relative influence of buyer and supplier bargaining power, government regulations, societal attitudes and lifestyle changes, information and communication technology (ICT),

support for the local community, and supply chain distribution economies are additional key driving forces that affect competitive success in the wine industry.

### *Competitive Strategies*

Crafting and executing strategies that are responsive to consumer preferences is critical to the success of small wineries. Consumers of wine seek specific *product* and *service* characteristics such as *product quality*, *price*, *a reputable brand*, *sensory qualities* (i.e. taste and smell), *bottle design*, *packaging*, *labeling*, *convenience* (e.g., screw cap versus cork screw), *environmental attributes* of the grape and wine production processes, and *relative speed* when conducting purchase transactions. The consumer's perception of *quality* of wine is in turn influenced by the *variety of grapes planted*, *taste*, *age*, *price*, *place of origin*, *distribution channel*, and other related dimensions. *Product differentiation strategies* that capture *quality features* sought by consumers are a key component of the competitive strategies being pursued by small wineries.

Competitive strategies for wineries are driven by *market positioning* and *branding strategies*. In *market positioning strategies*, the *selling price* determines the perceived value of the wine. Price serves as a key value indicator especially when wine is used as a gift or served as part of the menu in exclusive social events. Price delivers perceived value and makes it easy for consumers to decipher cheap versus expensive wines as the latter have a unique appeal to customers. *Pricing strategies* are a central pillar for competitive strategies for small wineries and price influences substitution possibilities.

Competitive strategies in LWSC are also associated with creative *branding strategies* such as using the *place of origin*, *history*, *eco-labeling*, and *trust* to gain a competitive advantage and capture increased market share (Loureiro 2003). Product origin and authenticity are key elements sought by wine consumers; although intangible, such attributes can build *trust* and *reputation* in LWSC (New, 2010). Furthermore, gains in competitive advantage could arise through the performance of *additional marketing services* and, again, *building trust-based relationships with buyers* (Abatekassa and Peterson 2011). In that respect, wineries catering to local markets can derive competitive advantage through *image and reputation strategies*. Consumers are known to exhibit loyalty to certain wine brands and are willing to establish long term relationships with wineries of their choice. Therefore, the successful commercialization of local wines depends on a mix of competitive strategies such as *product differentiation*, *market positioning*, *wine branding*, and the cultivation of *trust-based relationships* and control of *positive image and reputation* along the supply chain.

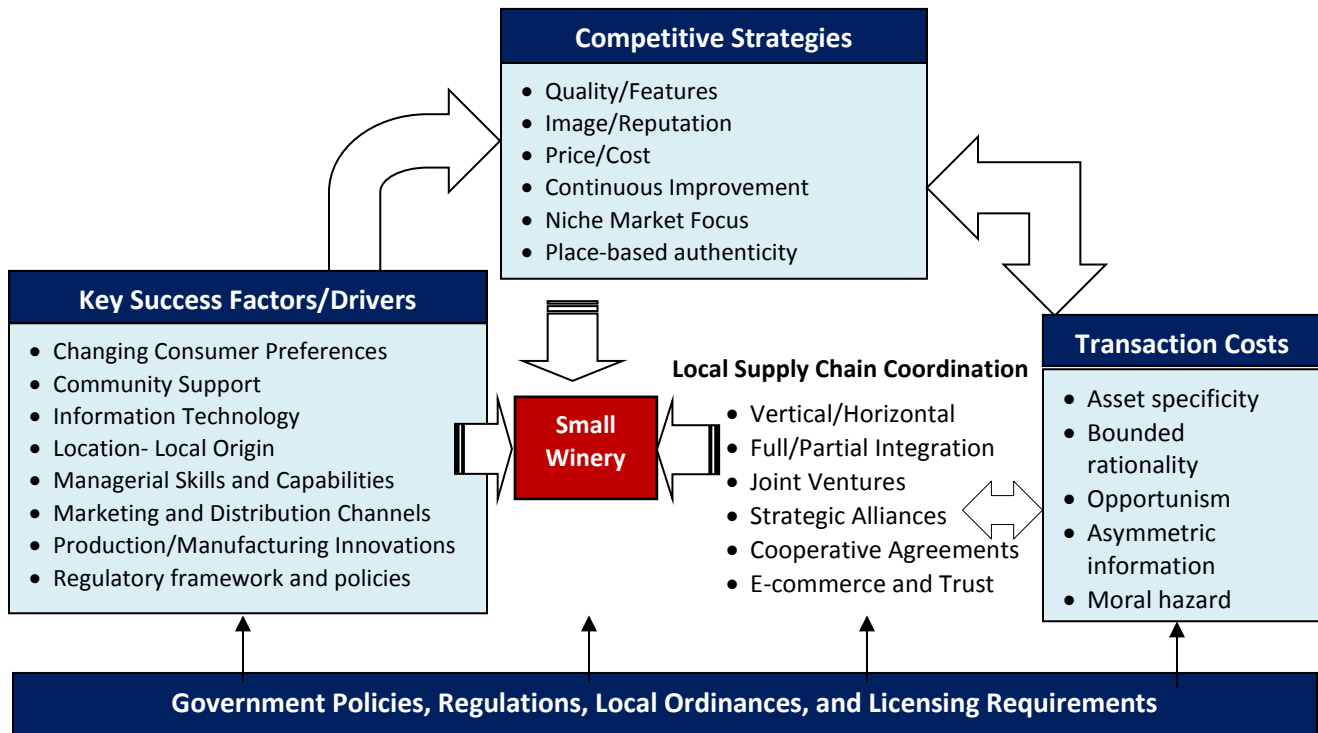
Just like wines in global supply chains, the *aesthetic value of local wines* is provided by a unique combination of product characteristics (i.e., taste, smell, packaging, labeling, and convenience to stimulate consumer sales. Demand for wine is driven primarily by its "customer value" bundle which is obtained by aligning product characteristics and buyer preferences. According to Foster et al. (2002), product quality and product condition are the top ranked attributes for Chilean wine purchases by US importers. Loureiro (2003) noted that *appellations of origin* (such as Napa Valley wines) are gaining in importance as a competitive marketing strategy in the US wine industry. Market competitive and coordination strategies (i.e., vertical integration, strategic alliances, trust-based partnerships, etc.) that align *product characteristics* (supply side) to *buyer*



preferences (demand side) have a direct impact on the level of transaction costs facing buyers and sellers in the wine industry.

*Transaction Costs in Local Wine Supply Chains*

Transaction costs for wine are high, and failure to account for both transaction and storage costs when trading wine tends to overstate the value of wine investments (Fogarty 2007). Transaction costs are the frictions in market exchange that arise from information asymmetry, bounded rationality, asset specificity and uncertainty. Information asymmetry is associated with unequal access to information between parties to a market exchange. Wine entrepreneurs face market demand uncertainty due to consumers’ lack of perfect information about product characteristics (i.e., prices, quality), location of buyers, and the behavior of both competitors and suppliers.



**Figure 1.** Conceptual framework for a local wine supply chain, 2010

State government regulations affecting Kentucky wineries, such as shipping regulations, licensing requirements and local ordinances involving consumption and sale of alcoholic beverages, impose uncertainties and raise transaction costs for wine entrepreneurs. Internet-based marketing of wine that involves social networking, blogs, vlogs, interactive e-commerce and the use of mobile broadband to facilitate transactions (i.e., mobile commerce) has gained ground (Thach 2009). The use of these innovative Internet-based marketing tools could potentially lower transaction costs across all segments of the wine supply chain and thereby increase margins of local producers. The need to increase transparency and lower transaction costs is associated with increasing use of bar codes that can be read by mobile phones and Radio Frequency Identification (RFID) tags to reveal product location and condition along the supply chain. In

California, some wineries use codes that can be entered on a website to verify authenticity of their wines and enhance market coordination with loyal customers. Such marketing approaches lower transactions costs and are beneficial to potential customers for AoLW who may be inclined to order their favorite wines from the AoLW website.

Wine consumers face transaction costs as wine has *credence attributes* that can only be determined after purchasing, hence the need for wine tasting and increased market coordination. Small wineries selling directly to consumers or to local markets are able to reduce these transaction costs by bringing consumers to the farm to see and taste for themselves the authenticity of the brand and through samples to and tastings at local retail outlets.

Wine production presents a unique case of the intersection of *horizontal* and *vertical coordination* in the food system. Investments in a winery typically involve grape production and harvesting, processing, bottling and packaging, storage, shipping and product marketing along the supply chain. Wine market coordination entails forging strategic alliances, joint ventures, and contract agreements with suppliers of key raw materials, such as wine barrels, wine bottles, and label designers among others. In addition to such forms of *market governance*, both vertical and horizontal integration enhance a firm's innovation behavior, lower production and transaction costs, and can boost the profitability of small wineries (Karantininis et al. 2010). Therefore, should the owner of AoLW reorganize the local wine supply chain? What strategic partnerships should be developed with other industry stakeholders? In what ways should the owner improve the current use of ICT and social media? What investments should be made, if any, to enhance the performance of the wine supply chain?

## Data Collection

This paper is based on a case study approach, which has been proven to be an important research tool for the agribusiness industry (Abatekassa and Peterson, 2011; Bitsch 2005; Stern et. al. 1998). This approach was deemed appropriate as it helps to explore, describe, and understand a local wine supply chain including the various actors and their inter-relationships. This case study was selected for the following reasons, (i) winery location (ii) its relative success in the industry, (iii) its use of a place-based versus conventional marketing strategy, and (iv) the willingness of the entrepreneur to share his successes and challenges with the researcher. Three visits to AoLW were conducted during 2007, 2008 and 2009. During the visits, which were in the fall and spring, farm tours were conducted by the owner who is directly involved in making all production and marketing decisions. During the visits, information was gathered on production and marketing strategies, new investments, and challenges facing the winery. The researcher visited AoLW on three separate occasions as a guest in the family restaurant facility during the study period. Additional information was obtained on the winery's website, and a questionnaire mailed to the owner in October 2010 was used to verify information collected during earlier visits to the winery. The questionnaire covered farm demographics, motivations for starting the winery, wine information sources, and market competitive strategies.

### *Study Limitations*

There are four major limitations to this study. First, the information provided by the owner might suffer from self-bias. Second, the owner operator might not be highly skilled in all the functions and operations of the different stages of the wine supply chain. This might mean that information provided may not be technical in nature. Third, the study does not provide comparative information of similar wineries at the time of the research. Fourth, it is difficult to establish causal relationships or make statistical generalizations when using a case study approach (Abatekassa and Peterson, 2011). Despite the afore-mentioned limitations, case studies generate useful detailed information that can be used to make key tactical, strategic and policy decisions.

## **Results and Discussion**

### *Description of the Local Wine Supply Chain*

AoLW is fully vertically integrated as the operator is actively involved in all decisions on grape production, harvesting, processing, bottling, storage, distribution and marketing. The operator demonstrates a sound knowledge not only of the farm, but its ability to sustain the competitive business of wine production and marketing. AoLW has established collaborative trust-based relationships with suppliers of key raw materials such as wine barrels (i.e. French Oak and Kentucky white oak), bottles, plastic bottle caps, and labels. Down-stream industry participants include ten wine tasting centers and distributors that are located in various parts of Kentucky. Geographically dispersed customers interested in AoLW wines can visit a local tasting center to try their wines. Figure 2 illustrates AoLW supply chain, including the key actors, market outlets, and the degree of market integration involved. According to the company website, AoLW has wine tasting centers and distributors that are scattered around rural towns in the state. AoLW wines are sold to the final consumer at a number of retail outlets including Kroger supermarkets, CVS pharmacies, liquor stores, gift shops, and inside the restaurant that is located on the farm property.

### *Agribusiness Competitive Strategies for a Local Wine Supply Chain in Kentucky*

#### **Vertical Integration Strategies**

One of the objectives of full vertical linkages in local food systems is to strengthen the link between farm gate prices and retail prices. Most of the wines produced by AoLW are sold on their farm (i.e., restaurant and gift shop), tasting rooms, and directly to local retail stores (i.e. supermarkets and pharmacies). Direct marketing of wines minimizes the transaction costs of producers and consumers and eliminates the marketing margin that is usually extracted by middlemen as is the case in conventional supply chains. AoLW's wines are also sold in various liquor stores with the owner directly involved in launching new wine varieties at these locations.

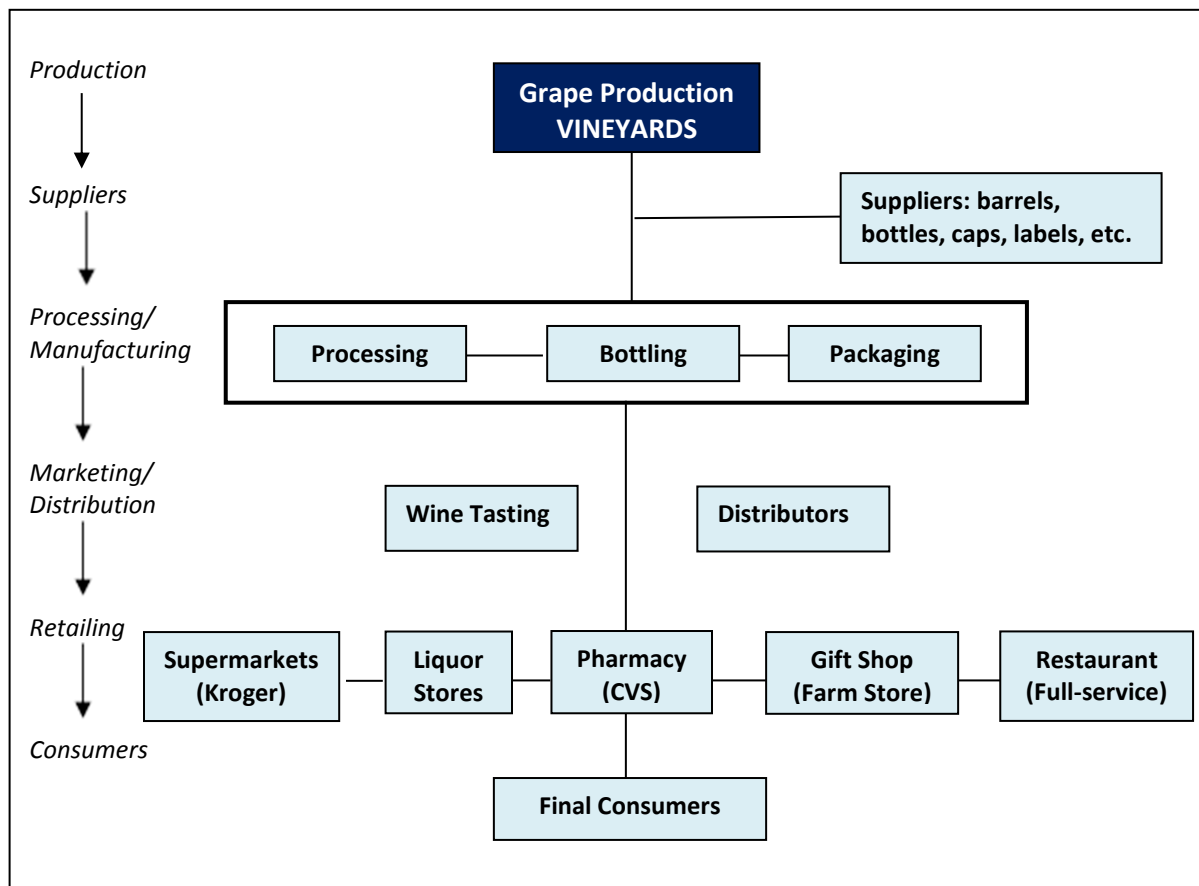
#### **Agri-Tourism Strategy.**

The management strategy of AoLW involves integration of agri-tourism activities as part of its overall competitive strategy. The agri-tourism venture consists of community-oriented programs

that involve organized visits to the vineyard, wagon rides, panoramic views of Madison County, tours of the state of the art commercial production and bottling facility, a gift shop, a wine tasting room, and a full-service restaurant with catering, banquet, and reception facilities. In addition, picnic dinners, wildlife (e.g., wild turkey, deer, butterflies, etc.) and sunset viewing are available forms of agri-tainment at the AoLW.

**Market Positioning Strategy: Kentucky Proud Label**

The AoLW is positioned as an authentic Kentucky experience. According to the operator, their wines are “made with pride and love from grapes grown in the fertile grounds of central Kentucky.” This market positioning strategy has led to the sale of wines and related merchandise using the Kentucky Proud label in gift shops and wine tasting rooms. Kentucky Proud is a statewide initiative that promotes the marketing of safe, fresh and nutritious food products that are grown, processed and packaged in Kentucky ([www.kyproud.com](http://www.kyproud.com)). The marketing slogan for the Kentucky Proud label, which has a relatively high recognition, is “nothing else comes close.” Prospective members are required to complete an application form from the Kentucky Department of Agriculture by listing their locally grown, processed and packaged products and agreeing to abide by the Kentucky Proud logo guidelines. Upon approval, members pay a royalty fee and are allowed to use the Kentucky Proud logo to market their products.



**Figure 2.** Description of Acres of Land Winery Supply Chain, 2010

The AoLW restaurant uses products and ingredients purchased from other local farms and producers who participate in the Kentucky Proud program. These products include ice creams, cheese, honey, jams, and sausages. The Kentucky Proud website provides marketing intelligence on other participating wineries and their respective locations in Kentucky. The key attributes for the Kentucky Proud label are low food miles, fresh, local, nutritious food, and building a sense of community. By marketing the “true taste of Kentucky,” this message corresponds to AoLW’s mission and goal of selling authentic Kentucky wines. As already highlighted, there are retail outlets for AoLW where new consumers can sample wines at numerous tasting locations spread around the state.

### **E-commerce Marketing Strategy**

Online marketing enables AoLW to market its wines on an interactive website. Customers visiting the AoLW website are able to pay for their favorite wines using credit or debit cards. The website has been in operation since 2008. Kentucky’s participation in the MarketMaker™ website program complements AoLW’s wine marketing strategy. The Kentucky MarketMaker™ is an interactive online portal designed to connect local food producers with newly emerging markets. It is based on a geographic mapping system that locates agribusiness producers and consumer markets in Kentucky. The initiative was first launched in Illinois in 2004, has now extended to 13 states, and is considered one of the most extensive collections of searchable food industry data in a given area in the US. Kentucky MarketMaker™ provides potential customers with information on various wineries and their locations throughout Kentucky. AoLW can be identified by visiting its website ([acresoflandwinery.com](http://acresoflandwinery.com)) or the Kentucky MarketMaker™ website ([ky.marketmaker.uiuc.edu](http://ky.marketmaker.uiuc.edu)). In addition, the use of mobile Internet broadband enables motorists and other travelers to google the location of AoLW in real-time thereby increasing its captive market.

Consumers are paying more attention to the origin of their food, and reading about the winery, its history, location and award-winning products enhances their bond with the local wines. Further, AoLW is available on *Twitter*, *Facebook* and *YouTube*. The use of real-time networking strategies demonstrates the entrepreneur’s innovativeness and commitment to modernize the winery’s marketing strategy and interact with a broad segment of its customer base beyond Madison County, Kentucky. The use of social networking tools and related ICT in agri-tourism is growing rapidly and is considered a win-win strategy for gaining competitive advantage and collaborating with other supply chain actors. Using social media tools gives AoLW the opportunity to constantly update its customers in real time about major developments at the winery including new wines and key upcoming events and contests. Furthermore, AoLW operates a toll-free number (866-714-WINE) to increase its linkages with a wider customer base. The use of e-commerce strategies is critical, especially at a time when consumers are more wary of some traditional marketing strategies, hence, agribusiness entrepreneurs need to strike a balance between innovative and intrusive advertising when using modern ICT channels (Phillips et al. 2009).

## Market Pricing Strategies: Price Discounting

In a recessionary economy, consumers tend to pay close attention to the final price of any purchasing decision. Pricing strategy at AoLW involves the use of price discounts to boost wine sales. The following discount schedule applies to online wine orders: 3 bottles, 5%; 6 bottles, 7% and 12 bottles qualify for a 10 % discount. Those customers with exclusive membership in the “Wine Club” receive a 15% discount on the purchase of their favorite wines. The pursuit of a best cost strategy is one way of stealing ‘value conscious’ customers with low switching costs from established rivals and thus reinforces AoLW’s competitive advantage in the marketplace.

## Promotional Strategies

AoLW has adopted a variety of promotional strategies ranging from advertising on local television and highway billboards, to word of mouth, on-farm tours, gift cards, wine clubs and wine festivals. The local television channel runs a regular advertisement for AoLW. Along the I-75 south freeway, about 10 miles before Richmond, motorists are welcomed by a roadside “billboard” with AoLW advertised. The wine promotional strategy used by AoLW combines the marketing of “place of origin” and “romance”. A similar strategy has been used successfully in marketing French wines as a “unique blend of historical intangibles of romance and mystery” (Terblanche, et al. 2008). Another commonly used strategy is *membership in a wine club* where information is exchanged about the winery and its latest products. *Word of mouth* is a particularly powerful tool and the owner conducts tour groups and talks to clients dining in the restaurant about the history of the farm and the available wines in the gift shop. The owner is also involved in directly marketing the new wines to potential customers in local liquor stores. This provides customers an opportunity to not only hear the history of the farm, but they get to meet the individual responsible for the production of the wines. The owner ranks tasting rooms as an extremely important market outlet followed by liquor stores and supermarket chains.

Awareness about AoLW increases through its participation in a number of *wine festivals* and *competitions*. As already noted, the winery received numerous awards in both regional and international competitions. Of the competitions held between 2006 and 2007, a total of ten wine varieties received 23 awards and recognitions from Taster’s Guide International Wine Judging, Northern Kentucky Wine Festival, Taster’s Guide Wine Lovers Competition, and the Florida State Fair Wine and Grape Juice Competition. These awards range from silver to bronze medals. The various awards are indicative of the brand recognition, quality, and reputation of this winery. According to the owner, their success is based on a mission of “patience, craftsmanship, and pride.” Such recognition of local wine labels through the use of effective promotional strategies and market positioning is crucial given that imported wines account for one out of every four bottles sold in the US (Hussain<sup>a</sup>, et al. 2007).

## Corporate Social Responsibility (CSR)

Global and local supply chains are dealing with the rising importance of CSR as part of normal business practices. The organizational structure of AoLW’s “agri-tainment” business, comprising vineyards, full-service restaurant, commercial wine production and bottling facility, gift shop, wine tasting area, and community facilities, highlights the strategic importance of building

community networks and support. As a result, AoLW has forged linkages with local communities in a number of ways. First, the winery hosts free tours and internships for local students. Its community facilities are used for weddings as part of its investment in building social capital and community networks. Second, the winery provides full-service dining, catering, and banquet and reception facilities to promote its wines and relationships with the local community. Thirdly, picnic and wagon rides are designed to further cement relations of AoLW with the local community. Forging such direct relations with the local community is a dual strategy to sell wines and promote the sustainability of its business through building a positive societal image.

### **Diversification Strategies**

Diversification into a restaurant business is a key risk management strategy at AoLW. The full-service restaurant which opened in 2005, after renovating an old tobacco barn, is renowned for serving fresh locally-produced food. The use of place-based commitments is a central part of AoLW's branding strategy as a business whose values and culture are firmly rooted in the local community. Visitors to the restaurant are reminded by the owner that the vegetables were growing in the garden that morning. This diversification strategy is also driven by the notion that wine and food are a perfect combination. Informing diners that the vegetables on their plate, the grapes in their salad or the herbs in a sauce were picked a few hours beforehand engenders place identity and utility for their wines. The restaurant appeals to a wider customer base by serving pasta, seafood, chicken, pork, and beef entrees in addition to appetizers, soups, and salads. Information about restaurant hours of operation, lunch, dinner, beverages and dessert selections and special events is readily available on the winery's website. The wedding coordinator provides support services to weddings which also bring in additional income for the winery. The growth in farm diversification in Kentucky is similar to trends observed in Colorado where the average recreational income on farms is reported to have risen from \$16,009 to \$448,472 (compared to an average per farm increase from \$2,738 to \$7,786 in Kentucky) according to the 2007 Census of Agriculture (Phillips, 2010).

### **Challenges Facing Entrepreneurial Local Wineries: Business and Regulatory Risks**

In the United States, local wine supply chains are facing a number of challenges that include access to markets, inadequate market information, government restrictions, business risk, changing consumer preferences and societal attitudes. The following section briefly describes the specific challenges facing the AoLW.

*Dry county regulations:* The location of AoLW in Kentucky presents a challenge in that some counties are legally "dry counties," meaning the sale of alcohol is prohibited. Although Madison County is not a dry county, AoLW wine sales are negatively affected by this statute. In 2008, prohibition of alcohol sales in some dry counties was repealed, allowing wine to then be sold in

*Fire hazard:* In 2009, an electrical fault caused a fire that burned down the AoLW restaurant. This was a major setback for the owner-operators who were trying to build a profitable business

through full vertical integration. Before this incident, the tobacco barn was completely destroyed by a tornado in 1955. The cycle of business risks associated with the barn and its subsequent renovation into a full-service restaurant symbolizes the entrepreneurship and survival strategies for this family business partnership. Despite these challenges, a newly remodeled restaurant was reopened a year after the fire.

*Cork problems:* Wine consumers are generally concerned about the effectiveness of corks as they sometimes allow oxygen inside the bottle that in turn spoils the wine quality. Management at AoLW has responded to these potential cork problems by investing in bottles that use plastic caps or plastic corks. The quality of the wine is critical to the stability of LWSCs and producers that consistently exceed wine quality expectations are likely to capture a relatively high market share. In contrast, wineries that compromise wine quality and taste are bound to face erosion of their market share in the wine industry.

*Procurement of barrels:* Aging of the wine depends on, among other things, the variety of the grapes and the type of barrels used. The barrels used by AoLW have a proven record of storing wine to develop its appropriate taste, after-taste and dryness. The key challenge is the relatively high cost of purchasing wine barrels given that French Oak barrels cost \$1,000 each and Kentucky white oak ranges from \$250 to \$300 per barrel. Bulk purchases of such barrels could potentially reduce the market price somewhat.

*Slow economic growth:* Wine is considered a luxury by most consumers. Generally, slow growth of the US economy between 2008 and 2010 resulted in consumers tightening their budgets leaving little discretionary income for luxury goods. Such unexpected economic fluctuations present pricing challenges for a small winery that is striving to reap a decent profit by charging economical prices for its wines. AoLW offers various price discounts to its customers as a strategy to remain competitive.

*Licensing requirements:* The selling of wines at wholesale or retail prices in Kentucky requires special licensing. Although AoLW sells wines in its gift shop and through its website, it had to meet strict regulations before that permission was granted. Licensing requirements are part of the transaction costs small wineries in Kentucky have to overcome before they can become fully competitive and sustainable in the long-term.

*Marketing challenges:* Place of origin has been used historically in global wine markets and continues to play a significant role today (Terblanche et al. 2008; Atkin and Nowak, 2007). However, these famous geographical indications, like Bordeaux in France and, more recently, Napa Valley in the US, have been based in traditional wine-growing regions that have built their reputations over decades. Wineries in non-traditional wine-growing regions, such as Kentucky, are instead appealing to consumers who live in or travel through the region and are attracted to a product that is authentically from that locality. With local food systems, tying the final value-added product to a particular farm is critical for generating demand. For a small winery to succeed, its marketing strategy must maintain such brand identity and authenticity throughout the supply chain.



## Summary and Conclusion

Kentucky was home to the first commercial vineyard in the US (kentuckywine.com). Wine production ended with the passage of federal Prohibition legislation and tobacco production increased. The end of the tobacco quota program in 2004 led to an accelerated exit of tobacco farmers and their entry into alternative cropping enterprises. As a result, a resurgence of wine production occurred in Kentucky and the state now has over 60 wineries (kentuckywine.com) with a potential agri-tourism value of \$565 million (Glengariff Group 2005). This paper is based on a case study of Acres of Land Winery (AoLW) established in Madison County, Kentucky in 2003 when the family farm was converted from a burley tobacco-producing farm. The AoLW prides itself in making Kentucky's finest wine. Driven by a mission of 'patience, craftsmanship, and pride' the winery has integrated vertically across the different stages of production, processing, and marketing. Survival has been a result of commitment and sharp focus on selling a truly authentic Kentucky product. Vertical coordination led to the forging of strategic alliances and trust-based relationships with suppliers of barrels, bottles, wine labels and food ingredients for the full-service restaurant located on the farm. The owner of AoLW has deployed both competitive and coordination strategies in response to changing industry forces and a desire to reduce transaction costs. Investments in wine tasting centers around the state and participation in regional and international competitions have helped boost market awareness and a positive image of its wines. AoLW sells its wines at local liquor stores, supermarkets, pharmacies, the winery gift shop and restaurant, and through the company website.

This case study illustrates how a local wine operator deployed innovative product differentiation, effective branding, market positioning, creativity in building trust-based customer relationships, and enterprise diversification to grow market share and penetrate regional markets. Senge (2010) observed that in order to become sustainable, businesses and organizations need *technical innovation, management innovation, process innovation* and *cultural innovations*. The AoLW has created its own niche by selling the "history of its farm" and "romance". An innovative product differentiation strategy based on location-based attributes and the ability to invoke something more appealing and special as "selling romance" attracts customers from the local community and beyond. Such a mix of product differentiation and promotion strategy has earned AoLW an image of selling high quality wines and local community support, which is vital for it to stay ahead of its competition in the wine industry.

The AoLW operator has enhanced the market awareness and reputation of AoLW by winning regional and international awards, substituting more reliable plastic corks for the true cork variety, and diversifying operations by serving farm fresh vegetables and grapes in the restaurant, a treat for customers committed to eating fresh locally-produced foods. Clearly, AoLW is an example of a local supply chain that is striving to be entrepreneurial and responsive to buyer-driven needs and preferences. Therefore, AoLW has managed to achieve steady progress and success through a combination of competitive market-oriented (i.e., differentiation, place-based identity, and branding) and diversification strategies. In addition, effective supply chain coordination and integration has helped to lower transaction costs and reduce risk and uncertainties. Risk management strategies revolve around establishment of a restaurant on the farm and an agri-tourism venture with farm wagon tours and hay rides that provide additional income to expand and modernize the winery, which is the main enterprise.

Institutional and policy support from the state of Kentucky was vital to the development of the local wine industry. The state of Kentucky facilitated the development of small wineries and locally produced foods in particular through its *Kentucky Proud program*, *Kentucky Grape and Wine Council*, and the *Kentucky MarketMaker™* website. In some counties, the repeal of restrictive “dry county” regulations that prevented wineries from selling their products in local supermarkets, liquor stores, and other retail outlets has helped improve market penetration of local wineries. The AoLW benefited from the support provided by the Kentucky state government through its *Department of Agriculture* and other related institutions. However, challenges still remain in moving local wines across state lines which make it difficult to tap into more profitable regional markets. Licensing procedures to allow operators to sell wines from cellars are still a major constraint.

In today’s world, emerging local wineries have to compete with relatively large conventional wine supply chains. Small wineries are being challenged to become creative, flexible and quick to address consumer demand for product quality. Strategic partnerships, community networks, place-based identity and branding strategies are being used to develop these entrepreneurial LWSCs. The provision of an enabling institutional and policy environment is a key element in the development of the small wineries. Given the foregoing, a few important questions arise:

1. Did AoLW take full advantage of the market opportunities, facilitative environment, and social capital gains from the community linkages to enhance the development of LWSC and the marketing of their local products?
2. How well did the operator manage risk and uncertainty in the LWSC?
3. Do you think the entrepreneur has developed effective risk management strategies to ensure AoLW’s future survival and sustainability?
4. Given that market intelligence and real-time decision making play a pivotal role in agribusinesses competitiveness, is AoLW well positioned in the market place to realize full benefits of modern ICT-based channels such as e-mail, *Facebook*, *Twitter*, and *YouTube*, to appeal to more customers?

Kentucky is not a traditional wine producing region in the US, yet it has the climate necessary to support the production of wine grapes. A core strategy to enhance broad-based entrepreneurship in the wine industry across the state needs to be explored. Some key issues to address include the identification of specific strategies for operators of emerging wineries to become *entrepreneurial*, *proactive*, *creative* and *innovative* in managing their LWSCs. Additional considerations include building *strategic collaboration* with key industry firms and customers to secure *competitive advantages* for small wineries and help promote the state as an emerging wine producing region. The final strategy approaches and recommendations will always be debatable. Nonetheless, the future survival these LWSCs will likely be affected by a clear articulation of strategies on how to promote market competitiveness, effective use of new technology innovations, development of industry and local community partnerships, and the ability to respond swiftly to changing consumer preferences.

Finally, LWSC are growing in importance in the US and are beginning to receive significant attention from consumers, policy makers, and researchers. In terms of future studies, research is required to; (i) better understand the impact of modern ICT in procurement, promotion, distribution, marketing, and customer relationship management in LWSC, (ii) examine consumer willingness to pay for environmental and place-based attributes in LWSC, (iii) analyze strategic trust-based or value-added partnerships such as the Kentucky Proud label and its potential to improve the performance of LWSC, and (iv) examine the competitiveness and sustainability of LWSC and the implications of upgrading to regional markets.

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## Appendix 1

### Fact Sheet: History of Kentucky Wine Industry

Kentucky was home to America's first commercial wine industry that was established in 1798. The first wine maker, Jean-Jacques Dufour started the first winery in the "Athens of the West" now Lexington. With support from local businesses, the Kentucky Vineyard Society was formed and the so called "First Vineyard" was planted in 1803 in what is now Jessamine County. The first vintage was sent to Thomas Jefferson, who was then the President of the United States.

During its early years, the wine industry faced numerous problems and challenges including the Civil war and crop damage from vine diseases. By late 1800, Kentucky was ranked the third largest grape and wine producer in the United States. The Prohibition Act resulted in Kentucky's grape and wine industry going out of business and farmers switched acreage from grapes to tobacco production.

Tobacco settlement funds from the Fair Equitable Tobacco Reform Act of 2004 have proved an asset for Kentucky farmers who are now shifting from tobacco cultivation into the winery business. Many grape varieties can be grown in Kentucky. However, American varieties are the easiest to grow, due to their hardiness, and insect and disease resistance, while European *vinifera* varieties are the most difficult, due to susceptibility to botrytis bunch rot, downy mildew, powdery mildew, and crown gall. Kentucky wine is also made out of American-French hybrids.

Kentucky offers two kinds of winery licenses: the Farm Winery License and Small Winery License. The Kentucky Vineyard Society promotes interaction and information sharing between buyers and growers of wine grapes. In addition, Kentucky wines are marketed using the *Kentucky Proud* label, a state-led marketing initiative designed to promote local products. Wine production in Kentucky is supported by a number of industry associations including Kentucky Grape and Wine Council, Kentucky Vineyards Society, Kentucky Growers Alliance, Western Kentucky Grape Growers Association, and the Northern Kentucky Vineyard and Winery Association.

To date, Kentucky's wine production is flourishing. The state has over 113 grape producers and more than 60 wineries, up from about just 15 five years ago. The Kentucky wine sector, with an annual output of 100,000 cases (or more than 200, 000 gallons) has seen tremendous growth over the past decade and is set to grow in the future. The grapevine acreage has risen exponentially from 67 acres in 1999 to about 600 acres today ([kentuckywine.com](http://kentuckywine.com)). The state has comparative advantage in its climate, soils, and beautiful agricultural scenery which is amenable to investments in grape production, wineries, and agri-tourism businesses in general.

The state's wineries offer diverse entertainment including wine tastings, gift shops, local-foods restaurants, concerts, weddings and other social events attractive to visitors. The MarketMaker™ website is a useful tool helping potential visitors locate Kentucky wineries while traveling across the state. Kentucky wineries are prospering and adding excitement to wine consumer's experience in the state via annual wine festivals and wine trails. Finally, Kentucky wineries have received local, national and international recognition and the state is poised to become a key player in the small wineries industry.

#### Sources.

- a. Kentucky Department of Agriculture
- b. [kentuckywine.com](http://kentuckywine.com)

## Appendix 2

### Fact Sheet: Case Study of Acres of Land Winery Inc.

#### The 8 Core Elements of Local Winery Market Positioning Strategies

1. **Agri-tourism Marketing Strategies**
  - Organized visits to vineyard
  - Tours of commercial production and bottling facility
  - Wine tasting tours, picnic dinners, wildlife, and sunset viewing
2. **Corporate Social Responsibility Strategies**
  - Business sustainability
  - Business ethics
  - Local culture - geographic origin and place identify
  - Building community networks and support
3. **Diversification Strategies**
  - Gift shop
  - Restaurant business
  - Weddings and social events
4. **E-commerce Marketing Strategies**
  - Interactive website- credit card and debit card transactions
  - Email - customer list serve
  - Kentucky MarketMarker™
5. **Market Pricing Strategies**
  - Direct marketing – restaurant and gift shop
  - Volume discounts
  - Membership discounts - “Wine Club”
6. **Market Promotional Strategies**
  - Billboards
  - E-newsletters
  - In-store product demonstrations
  - Kentucky Proud Label - “true taste of Kentucky”
  - On-farm tours
  - Television commercials
  - Toll-free number
  - Wine festivals and competitions
  - Word of mouth
7. **Mobile Commerce and Social Media Strategies**
  - Face book
  - You tube
  - Twitter
8. **Vertical Integration Strategies**
  - Full vertical integration- participation across all stages of the value chain
  - Partial vertical integration- maintain positions in selected stages of the value chain
  - Tapered vertical integration- mix of in-house and outsourcing activities in stage