Thriving between decline and crises

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Abstract:

In this paper, we explore the difficulties faced by SMEs and entrepreneurs within a fast-paced degrading environment such as a declining industry facing conjonctural crises. First, we explain the specificity of the wine market in the South of France which is determined by a specific combination of decline and crises. Secondly, we present an academic literature related to firms 'responses dealing with fast changing environments and difficult economic conditions. Then, we debate the significant challenges faced by small wine producers to succeed in a difficult economic environment.

Keywords:

Small wine producers, decline and crisis, strategic choice

Debating points: see chapter 3!

Introduction

According to Kitching *et al.* (2009: 5), "market economies are perceived as prone to over-accumulation as firms' pursuit of profit encourages continued investment until a situation of over-capacity is created, with too many goods and services produced relative to the level of aggregate demand. Over-capacity ultimately leads to a crisis of declining profitability, business failure, rising unemployment, and declining consumption – a 'consumption crisis' ". These authors also add that "access to credit can support consumption for a period of time, but not indefinitely. If credit becomes restricted, or consumers become unable to service their debt, then consumption is likely to decline with consequences for GDP and other macroeconomic indicators". According to us, "consumption crisis" is related to "crisis market" which characteristics are similar to those in hostile environments. Covin and Slevin (1989: 75) have defined hostile environments according to the following characteristics: precarious industry settings, intense competition, harsh, overwhelming business climates, and the relative lack of exploitable opportunities. They also defined hostile environments as a threat to small firm viability and performance. Important drop in firm performance is an obvious consequence during economic crisis (Antonioli, Bianchi, Mazzanti, Montresor and Pini, 2011). More generally, whatever will be the crisis contexts faced by small firms, they are mainly characterized by resources scarcity, especially financial resources scarcity suffered during *crisis economic times* (Schmitt et *al.*, 2010) and *hard economic times* (Eggers and Kraus, 2011). Moreover, according to Morin (1976), crises reveal dysfunction and nonsense localized in parts of a whole system. For instance, in a crisis industry, crises reveal deep rooted lacks, such as a common and ambitious prospective vision for the whole industry. As could assert the sociologist Michel Maffesoli, obsessed by the present – of the crisis that they don't understand – the majority of the actors of this crisis industry are losing their future. In fact, instead of calling for imagination and efforts towards necessary changes, actors are absorbed by the emerging and growing difficulties in the industry.

In the first part of this paper, we present the specific characteristics of the wine industry in the Languedoc-Roussillon region, located in the south of France, and the effects of the market crisis on the behaviors of small wine producers. In the second part, we investigate the academic literature related to strategic reaction of SMEs thriving between decline and crises. As "sources often provide little explanation of why businesses adapt in the ways they do, the conditions that enable, or constrain, particular adaptations, or the specific factors that affect performance outcomes" (Kitching et *al.*, 2009: 3), we introduce debating points in the third part of this paper. We develop arguments to explain the gap between fast-paced changing reality and stable misperceptions of reality by the actors of the declining industry. We try to explain why even if reference points become false, an "old" vision of the reality remains among the majority of actors of this industry.

1. The case of the declining Languedoc-Roussillon wine industry in South of France

Our study focuses on the small wine producers from Languedoc-Roussillon region, one of the largest wine producing regions in the world. Thirty years ago, the Languedoc-Roussillon region in the South of France represented the largest European area dedicated to table wine production, reaching a production of 30 millions hectolitres in 1980 (Chiffoleau *et al.*, 2006). However, since 2000, the wine industry of this region encountered increasing difficulties determined by a market disequilibrium between production and consumption. This structural crisis has determined several deep, dynamic changes that put into question the viability of the whole industry, including its current prevailing market paradigm (Montaigne, 2005). The causes of this structural crisis are quite well understood: the decrease of wine consumption in traditional producing countries, an increasing international competition, the absence of worldwide regulations regarding wine offer, and the inefficiency of the Wine Common Market Organization, whose activities are restricted to only one geographical area: the European region (Montaigne, 2005). Therefore, one of the most important consequences of this disequilibrium is an increased competitive pressure perceived by French wine producers at regional, national and international level (Cholette *et al.*, 2005). In 2001, France had the largest total wine consumption in the world - 3.4 billion litres, and a per-capital wine consumption of 57 litres. Despite these impressive figures, the decrease in French wine consumption was substantial, since 50 years ago the per-capita consumption was 120 litres per year (Echikson *et al.*, 2001). In addition, between 2001 and 2003, the French wine exports to the United Stated decreased by 34% in volume and 15% in value, and the French wine share in the UK market dropped from 43% to 25%, the demand shifting towards New World producers (Heijbroek, 2003). These trends had a negative effect on French wine producers' performance, the small wineyards being particularly hit by the economic downturn. The wine crisis in Languedoc-Roussillon became fully manifest in 2004 (Aigrain and Hannin, 2005) when the disequilibrium between production and demand was accentuated by the saturation of international markets.

Between 2000 and 2003, the economic context in the Languedoc-Roussillon region pointed towards a slow decline of demand and market attractiveness, followed by a suddenly aggravating crisis of supra-production, determined by complex inter-related factors that became manifest at regional, national and international level. The magnitude of this problem can be understood only when considering that for hundreds of years wine table production represented the main economic sector of this region, providing employment and resources for the majority of agricultural workers (Aigrain and Hannin, 2005). Moreover, in the Languedoc-Roussillon region, many small wine producers were organized as traditional family firms, with exclusive agricultural and production expertise passed down from one generation to the next (family businesses). In the past, the relatively constant level of demand did not require specific commercial or marketing skills to sell the produced wine. On the other hand, a large number of regional wine producers were traditionally specialised in table wine (Chiffoleau, Laporte and Touzard, 2006), characterized by a relatively low quality and brand power, which created additional barriers to successful strategic differentiation and market re-positioning (Anderson, 2004).

The regional wineyards were familiar with short-term crises, but in the previous cases the market growth restarted quickly, requiring no strategic action from producers (Aigrain and Hannin, 2005). As a result, when the new supra-production crisis became manifest, the wineyards kept producing wine, hoping for a quick economic turnaround. Therefore, the specificity of the wine market in the South of France is determined by a specific combination of decline and crisis, which determines significant challenges for small firms.

2. The strategic reactions of SMEs thriving between decline and crises

Previous studies questioned the ability of small firms to deal successfully with crises, economic decline and downturn. During economic crisis, managers are forced to deal with such perverse effects as hypercompetition, structural disequilibrium and lack of resources in a hostile business environment characterized by more threats and fewer opportunities (Covin and Slevin, 1989; Zahra and Covin, 1995). The crisis also modifies the structure of valueadded chains, the relationships and power balance between company, its suppliers, customers and partners, imposing a rapid rhythm of change characterized by unpredictability, risk and complexity (Mintzberg, 1979).

Previous research also makes contradictory predictions concerning the ability of SMEs to reverse the performance trend in decline and crisis situations. Confronted with rapid rhythm of change, some managers respond better than others, implementing strategic decisions that improve the performance of their organizations (Weaver *et al*., 2002), and thus increasing the chances of firm survival and success (Dess *et al*., 1997). According to Staw, Sandeland and Dutton (1981), the threat-rigidity principle explains slow managerial reactivity: when faced with significant and sudden threats, individuals are frozen into inaction, which results in cognitive rigidity. The managerial decision-making process is thus impaired and the firm is subject to failure. Harrigan (1980) argues that firms will find more difficult to deal with crisis than with decline, considering the gravity of competitive challenges.

Therefore, the situations of decline and crisis create different sets of challenges for SMEs: decline is characterised by a gradual, long-term reduction in market opportunities and firm performance, while crisis has quicker and more dramatic effects, influencing several areas of economic and social activity, and increasing competitive pressures. The devastating effects of this decline/crisis combination were enhanced by the lack of business insight of most small wine producers. In fact, the management structure of SMEs, which is often represented by a single person - the owner or the entrepreneur (Khan and Rocha, 1982), limits the capacity to rapidly and accurately identify the signs of economic downturn. This concentration of decision and control increases firm's reactivity to market challenges, but impairs the managerial perception regarding the evolution of the competitive environment. In these conditions, the decision-making process may be delayed or biased by individual cognitive limitations (Carson, 1985).

3. Main debating points

The difference in the magnitude of effects between decline and crisis impacts on manager's ability to identify, react and respond to market challenges. Many producers lacked the necessary expertise to understand the long-term consequences of the market failure, and the capacity to take decisive strategic action. Tichy and Devanna (1986) also explain that the slowly deteriorating environment such as a declining industry provide an insufficient alarm threshold for managers. When performance downturn is gradual "a serious response is never triggered, or at least not until it is too late to respond" (Hambrick and D'Aveni, 1988: 4).

According to us, here are the debating points of the paper. For instance, we chose to debate this specific point that "many producers lacked the necessary expertise to understand the long-term consequences of the market failure". We want to argue that slow responses from SMEs is also linked to a fast pace of deterioration that overtakes the capacity of small wine producers to fill the gap between reality and their perception of the reality. Moreover, we want to argue that the responsibility of failures is also collective and not only individual.

First of all, in the Languedoc-Roussillon wine industry, we have noted that there was no acceptation of a declining stage reached by the whole industry until December 2011 when the regional newspaper *Midi Libre* titled its first page: "Regional wine industry : the inexorable decline ?". Used to face and overcome so many market crises in its history, this regional wine industry was barely able to pronounce the word "decline", instead "crisis" is commonly used even if Aigrain and Hannin (2005: 27) used the word "faintness" rather than "crisis". Anyway, why to take into account so late the possible scenario of decline for this regional wine industry? Why the majority of the actors in this industry were still anchored in the old system (including inefficient European regulation tools such as uproots and distillation) expecting new trends of rising wine market prices in a globalized market?

Therefore, we would like to debate the following arguments all related to a crisis or declining industry.

<u>- What we should know and publicly post:</u>

As we consider that transparency is an important notion in crisis context, we have worked hard during four years to become specialists of this crisis wine industry. We knew we will have to advise small wine producers facing economic difficulties so we had to know what was exactly their industry in order to explore their possibilities of getting out of the regional wine market crisis. Therefore, the challenge was no more to gather and compare existing data but to go far beyond these data in order to be able to criticize them. It is exactly what happened. Looking for transparency, we found wrong forecasts in official charts, non updated or inaccurate data on websites and paper media, long time to market for certified quality and updated data. Obviously, we have observed that the crisis context has its own specificity. We could wonder how far old mindsets and mental representations which were partly or totally obsolete, were kept stable among the majority of actors of the industry thanks to wrong forecasts and non updated data? For instance, we can quote that in May 2011, we still could read on the regional website of one the most important French winemaker network named Vigneron Indépendant : « The area of the wineyard of Languedoc-Roussillon is the most important in the world with an area closed to 290 000 hectares » (source : www.vindusud.fr/frame.php). Nevertheless, in 2009, this area was already no more important than 246 000 hectares (*Source : Srise Languedoc-Roussillon – SAA*) and in 2010, this wineyard was already no more the first but the second area in the world following the Spanish wineyard of Castilla La Mancha with an area of 500 000 hectares.

- What we would like to know:

Another characteristic of the crisis is non aptitude for humans to describe with words what is happening in front of their eyes. If we try to define phenomenon, we often participate to hypnotize actors and to maintain the statu quo by leaving projects in limbo. It is what Le Brun (2009) named the hypnotic function of the language. For instance, by using oxymorons, we try to explain phenomenon but “zero growth” and “negative growth” obviously do not mean “growth” even if for sure it adds confusion to confusion. Moreover, even if according to Morin (1976) the concept of crisis itself seems to allow us to justify the fact that we do not understand the evolution of one particular situation, “crisis” is not similar to “decline”.

- What we cannot know:

In a declining or crisis context, what we should expect is the worst. In the fast-paced downward spiral, degradation, especially at a macroscale level, is non linear and therefore not straight visible. But if we consider threshold effects, the worst could be not so far. The pace of degradation can be accelerated as soon as parts of the declining industry have reached a particular threshold. This threshold can be difficult to measure but can play the role of a time bomb. For instance, if the resilience of small firms during hard economic times is linked to interactions between a certain number of small firms, under a certain number of small firms and interactions, the whole system is degraded and can disappear.

Conclusion

The difference in the magnitude of effects between decline and crisis impacts on manager's ability to identify, react and respond to market challenges. Therefore, we chose to debate the fact that many small wine producers lack the necessary expertise to understand the long-term consequences of the market failure, and the capacity to take decisive strategic action. We argued that the responsibility is also collective and not only individual as available information may be not updated, full of wrong forecasts reflecting a collective vision of the future of a regional wine industry that remains blurred.

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