Tbilisi 2022 Abstract Submission

Title
Veblen on Wine: Ahead of His Time?

I want to submit an abstract for:
Conference Presentation

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Keywords
Wine, Veblen, Veblen effect, conspicuous consumption, signaling, premiumization, consumer demand, luxury goods, prices, economic history

Research Question
How can Veblen's 1899 insights help explain consumer demand in the present-day wine market?

Methods
Analysis of multi-modality in a data set of more than 1 million retail wine prices across the U.S. from the Total Wine online sales portal; theoretical application of Veblen.

Results
We observe multi-modality in the frequency distributions of US wine prices. We find that the segmentation of the wine market into several price sub-segments is best explained by Veblen.

Abstract
The American economist and popular pundit Thorstein Veblen (1857–1929) is best known for coining the phrase “conspicuous consumption.” Veblen’s fame peaked in 1899, when he published his bestselling book The Theory of the Leisure Class and went on the lecture circuit. The central claim in Veblen’s work was that the vast majority of spending and consumption by affluent consumers is motivated by the desire for social status rather than by physical needs. Veblen observed that consumers with extra disposable income tend to seek out scarce or unique goods that are in vogue among upper-class aristocrats whose lifestyle such consumers wanted to emulate.

Veblen argued that when disposable income increases, the behavior of consumers across all classes becomes increasingly motivated by the aspiration to maintain or elevate one's social status by imitating the upper-class way of life in every respect, which means displaying "conspicuous waste" in one's lifestyle and conforming to the "canons of taste" in one's consumer preferences. In Veblen's work and elsewhere, the taste for and spending on fine wines and rare wines is often cited as a classic example of such "aspirational" consumption.

In recent years, results from a variety of blind wine tasting experiments have suggested that consumer demand for expensive wine may be better explained by packages, labels, and conformity with expert opinion than by the sensory qualities of the wine (Goldstein et al., 2008; Hodgson, 2009; Ashton, 2014). In spite of this apparent dissociation between price and sensory preferences, the 21st-century wine market has been flooded with thousands of new expensive, small-production wine brands, many of which have succeeded. These results are in line with Veblen's observations, more than a century earlier, that in a leisure economy where basic consumer needs are satisfied, firms seeking sustained profitability may increasingly compete on what Veblen calls "salesmanship (includes, e.g., needless multiplication of merchants and shops, ..., sales-exhibits, sales-agents, fancy packages and labels)."

In 1950, Veblen's theories were codified by the economist Harvey Leibenstein in a QJE paper entitled "Bandwagon, Snob, and Veblen Effects in the Theory of Consumers' Demand." Leibenstein (1950). Leibenstein's "Veblen Effects" are characterized by upward-sloping demand curves, where an increase in price causes an increase in demand. In introductory economics courses, Leibenstein's Veblen Effects are commonly cited along with Giffen Goods as the two known exceptions to the economic Law of Demand. In our view, however, although Veblen's work can be well applied to present-day markets, the demand pattern Leibenstein describes has little to do with the real world and even less to do with Veblen.

Veblen's prediction was not that an increase in price of a given good would cause an increase in demand for that exact good. Veblen did not predict upward-sloping demand curves, as Leibenstein did. Instead, the basic effect Veblen predicts is that in a market where most consumers' basic physical needs (food, water, shelter, heat, cooling, etc.) are met, the drive for social status dominates consumer demand.

Let's say that a consumer buys a Rolls-Royce instead of a Hyundai to impress his neighbors and feel better about himself. This purchase motivation, and the desire to spend a lot more for the Rolls-Royce, does not mean that raising the price of the Rolls-Royce will increase its sales. Nor does it mean that decreasing the price of the Hyundai will decrease its sales. Veblen simply asks why anybody would buy a Rolls-Royce when a Hyundai of equivalent size would serve their practical needs just as well. The choice to spend extra on a high-priced luxury good is not motivated by practicality: it is motivated by social signaling, by wanting to have the feeling of driving around like you're the Queen of England.

Collectors who buy rare and expensive wines, like collectors who buy rare and expensive cars, tend to pride themselves on not merely choosing a product because it's the most expensive. They pride themselves on expressing their own personal taste in their choices. Once they've made a choice of product, luxury consumers are as price-sensitive as anyone, and they might well haggle over price. A wine collector who sets their sights on a bottle of 2010 Château Margaux will seek out the lowest, not the highest, price for a case of that wine at auction (as long as it's believed to be genuine).

So the real Veblen effect (as we see it) does not express in an upward-sloping demand curve for an individual good. Rather, what Veblen centrally observes is that with increased disposable income comes a consumer shift from lower-priced to higher-priced goods of similar functionality. It is in their choice of the whole higher price range (one encompassing the acceptable group of classy blands reflecting the tastes of the aristocracy) that the desire to spend more just to spend more manifests.

In this paper, we apply our own interpretation of Veblen's original theory—untarnished by Liebenstein's tradition—to the present-day wine market. We analyze a data set of more than 1 million U.S. wine prices from the Total Wine website and observe multi-modality in the frequency distributions of US wine prices (shown with histograms). We discuss the segmentation of the wine market into several premium sub-segments, a phenomenon that is best explained by Veblen's theoretical framework of luxury demand. We also aim to correct some common misconceptions about Veblen’s theoretical stance, and to protest the misnaming of Leibenstein’s “Veblen effect” in economics.

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