

# Online Competition Brings Down Wine Prices In Local Stores

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New research suggests a good way to significantly reduce the price many Americans pay for a bottle of wine: knock down the trade barriers between states.

Researchers found that brick-and-mortar wine stores near one Virginia town charged significantly more than online stores in 2002, when interstate shipping of alcohol directly to consumers was illegal in the state. But the price difference shrunk nearly 40 percent by 2004, after interstate shipping was legalized.

“Consumers are better off when local stores have to compete with online sellers,” said Alan Wiseman, co-author of the study and assistant professor of political science at Ohio State University.

“Virginia merchants reduced their prices to meet online competition, and I think the same thing would happen in other parts of the country if the laws allowed.”

The wine industry is big business in the United States , and growing bigger. Wine sales in the United States have increased for 13 straight years, and totaled \$27.8 billion in 2006, according to the Wine Institute, an advocacy group based in California.

Wiseman conducted the new study with Jerry Ellig of the Mercatus Center at George Mason University . They published their results in a recent issue of *The Journal of Politics*.

The researchers were interested in the issue of interstate wine sales because it relates to the commerce clause of the U.S. Constitution. The clause states that Congress has the power to regulate trade activities between states. In general, that has meant state governments could not limit interstate sales of goods.

But the one exception allowed by law, Wiseman said, has been alcohol. Many states, such as Virginia, had prohibited direct interstate shipping of alcohol to consumers in their states, while allowing shipping within the state.

However, in 2003 a federal court ruled that, based on the commerce clause, Virginia could not discriminate against out-of-state shippers to favor those within the state. That forced Virginia to change its law to allow interstate shipping.

A 2005 U.S. Supreme Court decision essentially confirmed the federal court's ruling. Wiseman said other states have begun changing their laws to meet the Supreme Court's decision, or will soon have to consider such modifications.

The question is, what impact will the Supreme Court decision have on the market for wine in the United States? This study provides a glimpse, Wiseman said.

In July 2002, before the court decision, the researchers conducted a study on wine sales within a 10-mile radius of McLean, a wealthy suburb in northern Virginia, near Washington, D.C. They checked which wines were available and at what price at every wine retailer listed in the Yahoo! Yellow pages in that area.

Specifically, they looked for wines selected as “The Top 50 Most Popular Wines” in America's restaurants, as chosen by Wine and Spirits

magazine. They then compared price and availability of these wines with the same bottles available online.

In 2002, about 15 percent of these most popular wines were not available in McLean-area stores, Wiseman said, while all were available online. For the more expensive bottles, Virginia residents would have saved up to 21 percent per bottle if they could have shopped online and had the bottles shipped directly to them.

However, the wine market changed considerably by 2004, after the state of Virginia legalized interstate direct wine shipping to consumers. Brick-and-mortar stores dropped their prices substantially, shrinking the price differential between local stores and online stores by about 40 percent.

A key finding was that McLean area wine shops still charged more than online stores, Wiseman said – and the remaining price difference depended on how much it would cost to ship the bottles from out of state.

“The results suggest that brick-and-mortar stores were quite calculating in knowing how much more they could charge customers,” he said. “They knew that their prices couldn't be too far above out-of-state merchants, but that they could still charge a premium because of shipping costs.”

In 2002, the higher prices local stores charged customers were unrelated to shipping costs, showing that local stores did not have to worry about online competition, Wiseman said.

The researchers found that selection of wines didn't improve much after online (and out-of-state) competition was introduced. In 2004, 12.5 percent of the most popular wines were still not available in local stores near McLean, not much better than the 15 percent that were unavailable

in 2002.

From a political perspective, the study shows that the commerce clause really does have an important impact, Wiseman said.

“The commerce clause clearly facilitates a more efficient market,” Wiseman said. “When you eliminate interstate trade barriers, local sellers have to compete with out-of-state sellers and consumers benefit.”

Wiseman said the full effect of the 2005 Supreme Court decision has not yet been felt because states are still adjusting their laws to comply.

“There's going to be a lot of legal maneuvering because there is a lot of money at stake in the various parts of the distribution chain,” he said.

“There is still some ambiguity in the Court's decision, so there will probably be more litigation about what states can regulate and what they cannot.”

Source: Ohio State University

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