



Contents lists available at ScienceDirect

## Journal of Business Research



## Linking online niche sales to offline brand conditions

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## ARTICLE INFO

## Article history:

Received 5 February 2016

Received in revised form 12 July 2016

Accepted 18 July 2016

Available online xxxx

## Keywords:

Multichannel retailing

Channel substitution

Channel synergy

City of origin

Niche brand

Offline brand condition

## ABSTRACT

With the dramatic growth in the online marketplace, online retailers are keen to understand and leverage the interplay between offline environment and online sales. This study examines the influence of offline brand conditions on online sales of niche brands. Specifically, we investigate the proximity to the leading brand's headquarters, *city of origin*, and the extent of its offline distribution, *offline brand availability*. We also examine the moderating effect of offline affinity for niche attributes, *offline niche affinity*. Using sales data of niche brands, we find that brand share is higher in regions closer to the city of origin and where brand availability is limited. The category sales benefit from proximity to the city of origin and increased offline brand availability. This positive impact of favorable offline brand conditions on category sales is more prominent in regions with lower niche affinity. Finally we offer managerial insights for marketing practice.

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## 1. Introduction

Online retailers generally offer the same product assortment in every geography at the same prices; however, sales performance varies substantially across geographies (Bronnenberg, Dhar, & Dubé, 2009; Brynjolfsson, Hu, & Rahman, 2009; Choi, Hui, & Bell, 2010). Online companies are aware of the role that geography plays in such regional variation, and take into account local conditions when monitoring or planning online activities. For instance, Amazon.com keeps track of buyer locations to monitor local demand for its products (Banker, 2014). Zappos.com, an online shop specializing in shoes and clothes, went a step further and opened a showroom near its headquarters in Las Vegas. It was a measure not only to complement overall online operations, but also to offset the advantages of local competitors (Fox, 2014). Overstock.com, another online retailer in Utah that sells surplus merchandise at a discount, initially established its market presence by capitalizing on its proximity to large markets on the West Coast. It later expanded its influence to the East Coast by building a logistic center in Cincinnati (Demery, 2013). With the increasing importance of the online marketplace, companies are keen to understand and leverage the interplay between offline conditions and online sales performance.

Academic literature to date in economics and marketing demonstrates the importance of this area of research. The research has established that local conditions, such as target demographics, play a key role in explaining geographical variations of online performance (e.g., Bell & Song, 2007; Chintagunta, Chu, & Cebollada, 2012; Choi & Bell, 2011; Forman, Ghose, & Goldfarb, 2009). We contribute to the literature by expanding extant knowledge of how offline factors influences online performance. Specifically, we focus on three offline conditions, the proximity to the brand's headquarters, *city of origin*, offline brand distribution, *brand availability*, and offline affinity for a niche attribute, *niche affinity*, and investigate their joint impact on online sales performance.

First, city of origin of a company is a well-explored topic in economics. Bronnenberg et al. (2009), for instance, show that a brand enjoys a market share advantage in the region close to its city of origin; this effect diminishes with increasing distance. However, this finding has received little attention in multichannel studies, despite its potential contribution and easily accessible data. Second, the offline accessibility of brands is another topic well studied. Some studies find evidence for demand substitution between offline and online channels (Brynjolfsson et al., 2009; Forman et al., 2009), whereas others demonstrate channel synergy, where greater offline accessibility enhances online performance (Avery, Steenburgh, Deighton, & Caravella, 2012; Bell, Gallino, & Moreno, 2015). We examine which of these are more likely to be at work in our research setting. Finally, we investigate whether the two factors, city of origin and offline brand availability, are moderated by a third offline factor, local taste for a prominent category attribute.

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A strong liking for some attributes may intervene in the process of city of origin and availability of a brand influencing online sales at the regional level; that is, it can either intensify or mitigate the main effects.

We choose a research setting in which the category attribute is known to induce a highly polarized preference at the individual level (i.e., organic; Schifferstein & Ophuis, 1998). Moreover, there is a large variation across regions in the observed preference. The sales data for a specialty niche category (in our case, organic disposable diapers) is not only ideal for testing our hypotheses, but also interesting in other aspects. First, a recent trend in the consumer packaged goods (CPG) industry shows a proliferation of specialty products designed for micro-segments, and continuing growth in e-commerce for such products (Wall Street Journal, 2015). The trend seems to be in line with recent studies demonstrating that online shoppers are relatively wealthier, better educated (Smith, 2015), and willing to pay more (Lee, 2011). Thus, specialty niche categories deserve attention in their own right. Second, niche brands might benefit from a significant growth and change in contrast to relatively established mainstream markets dominated by mass-market brands. This market situation allows probing for answers to questions such as “how do markets (niche categories) grow?” while most brand managers ask “how do brands grow?” (often at the expense of competing brands) (Sharp, 2010).

We measure the market performance of specialty brands using category sales and brand share to reflect the market situation in the niche category, and investigate two outcome variables in a model that interlinks the two processes. The empirical results indicate that the main effects of the city of origin and brand availability significantly affect online brand performance. Specifically, proximity to the city of origin improves both brand share and sales of the category as a whole; greater offline accessibility of the focal brand increases category sales, but reduces brand share. Interestingly, the city of origin effect is not limited to offline retailing but transcends to the online sphere. Additionally, greater offline accessibility of the focal brand benefits other niche brands in the same category, and thus significantly contributes to the growth of the niche category itself.

Furthermore, category-level offline affinity for the niche attribute, that is, organic, moderates the effect of the two offline brand conditions on category sales, whereas it exerts no influence on relative brand share. Greater proximity to headquarters increases category sales, and this positive effect of the city of origin is mitigated by high local affinity for the attribute. In addition, a larger number of offline stores selling the focal brand leads to higher category sales because the stores function as showrooms for this lesser-known niche category; this positive impact becomes smaller when local markets have a strong preference for the niche attribute. These findings add interesting insight to the literature: the beneficial influence of offline conditions on the online niche category is more prominent in regions with less existing affinity for the niche attribute.

The rest of the paper is organized as follows. First, we discuss the conceptual framework and the related literature, and provide hypotheses. We then introduce data and describe the empirical model. Next, we present the results from the hypotheses testing. Finally, we discuss the contributions of our study to the literature, as well as the managerial implications for both online retailers and managers of niche brands.

## 2. Literature and hypotheses

Our study adds to the growing body of literature that provides an understanding of the relationship between the local environment and online sales. While online marketing actions influencing online brand sales are a well-researched area, cross-channel influences are an on-going area of investigation. In particular, offline influence on online sales of smaller brands has largely been overlooked. We contribute to this literature by focusing on the under-researched topic of niche brands.

We focus on specialty niche brands in particular. The term “niche” has been used laxly in practice, sometimes referring to any brands that have low market share (for instance, see Anderson, 2006). We follow the concept of niche used by Kahn, Kalwani, and Morrison (1988, p. 384); niche brand is the kind of goods that a small segment of the market requires due to its refined and more clearly defined needs. This kind of niche brands are well characterized by a distinct attribute (e.g., cavity-prevention focused toothpaste, Greek yogurt within the overall yogurt category), and often form their own niche market in which several brands of a similar core benefit compete. Brands within this niche market are considered niche brands because they possess niche characteristics, not necessarily because they have low market share as compared to the mainstream brands (i.e., products that appeal to a larger group of customers and enjoy greater market share).

Our study adds to the understanding in the following fields of study by developing and testing hypotheses: 1) the city of origin effect of niche brands and online sales performance, 2) the effect of offline brand availability, and 3) the moderating role of offline niche taste (affinity for niche attribute). Online performance is operationalized in two dimensions: niche category sales and niche brand shares. In developing our hypotheses, we first discuss brand share, as this topic has more related theories and evidence, and then category sales. Fig. 1 presents the framework for the hypotheses proffered in the following sections, and Table 1 discusses the related literature and our contributions.

### 2.1. City of origin of niche brands

Previous studies on the city of origin show that regions closer to the brand headquarters benefit from greater brand performance. Bronnenberg et al. (2009) show that the share advantage of a brand (defined as the share difference relative to the most distant market) is greater in regions closer to its city of origin. This share advantage is attributed to the early entry effect and the consequent improvement in brand quality perception. Kalnins and Lafontaine (2013) also demonstrate that the longevity of a business is negatively proportional to the distance to its headquarters. They propose that ease of monitoring and local information asymmetry are the underlying drivers. Similarly, Choi, Hong, and Jeon (2013) investigate sales data in the liquor market and show that the city of origin effect is present, and enhanced by a stronger local identity. These studies improve our understanding of the city of origin effect in offline retailing, but do not extend the scope of their research to online retailing, particularly for niche brands.

Unlike mainstream brands, niche brands generally have small offline sales revenues, and in turn, limited offline presence and influence. However, they serve customers who have clearly defined preferences and benefit expectations (Kahn et al., 1988). Due to the strong appeal of the value proposition of such niche brands, there is a demand-side pull that compensates for the limited physical influence. Thus, we postulate that the city of origin effect is not limited to mass-market brands but can be applicable to niche brands as well.

Studies on social influence through physical proximity provide insights on how the city of origin effect in physical domain manifests online. Physical proximity leads to imitative behavior for offline purchasing among neighboring households (Conley & Topa, 2002; Grinblatt, Keloharju, & Ikäheimo, 2008; Yang & Allenby, 2003). However, the neighbor effect is not limited to offline buying; imitative behavior due to physical proximity manifests in online buying behavior, as evidenced in previous studies for online sales of consumer packaged goods (Bell & Song, 2007; Choi & Bell, 2011; Choi et al., 2010). In a similar vein, physical proximity to the city of origin may foster social interactions among target consumers who shop online, subsequently raising brand awareness, enhancing quality perceptions, and ultimately, improving online brand performance. Accordingly, city of origin effect transcends physical boundaries and affects online market performance.

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