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The effect of information exposure of contract manufacturing practice on consumers' perceived risk, perceived quality, and intention to purchase private label brand

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1. Introduction

The private label industry is a growing industry with the largest market for food and beverages in North America and Europe. In the developing countries, private labels have also been getting popularity despite the low penetration rate (Collins and Bone, 2008). Private label products were once perceived as low price version of national brands which would sacrifice quality for cheaper price. Today, private label brands (PLB) are more connected with customer trends and no longer associated with low price and low quality (Nielsen Global Private Label Report, 2014). In fact, there are tiers in the world of private labels that distinguish the premium and the low-end private labels. Despite such progress, the majority of mainstream consumers still perceive the low price benefit of private labels, especially when the economy is not in its best shape.

According to Datamonitor (2008), an international company providing market intelligence and data analysis, reported that consumers traded down their consumption behavior by switching from their favorite national brands to private label brands, as response to the declining economic condition. According to a report of Global Market Trends 2018 by the Euromonitor, respondents aged between 30 and 44 years old (those with young children) were more likely to increase their purchase of private label brands at 16%, signaling that they were seeking ways to make their money more well-spent (Euromonitor, 2013). This highlights that consumers still view private labels as less expensive substitutes to national brands. While one may suggest that the trading down to private label happens only in the recession, the latest report by IRI still finds the consumers are still turning to private labels, even in the stable economy – especially for the Millenials (IRI, 2017).

Private label products are defined by The PLMA (Private Label Manufacturers' Association) as "all merchandise sold under a retailer's brand, which can carry the retailer's own name or a name created exclusively by that retailer. In some cases, a retailer may belong to a wholesale group that owns the brands that are available only to the members of the group." The manufacturers of private label may fall into one of the four categories: (1) large national brand manufacturers, (2) small manufacturers specializing in certain product lines, (3) major retailers and wholesalers who own manufacturing facility, and (4) regional brand manufacturers who manufacture private label products for exclusive markets.

National brand manufacturers would normally use their skills and excess production capacity to produce private label products. This practice – known as contract manufacturing – is believed to be able to reduce risks and provide opportunity to maintain high level of production for the manufacturers (Department of Agriculture and Agri-Food Canada, 2010). Contract manufacturing is nothing new to producers, wholesalers, retailers, or those who are familiar with the retail industry. From the perspective of customers, however, this practice may not yet gain popularity and therefore, customers may not be aware of the existence of contract manufacturing practices. Not until recently that information on contract manufacturing practices by national brand manufacturers has been shared and discussed openly in the media, more specifically on the Internet; thus, making it no longer secret to the public. Contract manufacturing that involves national brand manufacturers producing the same product to be sold under private label brand has been kept in the shade from customers' view. Information exposure of this issue to public may trigger various responses. Therefore, this paper aims to examine consumers' reaction following an exposure of information about contract manufacturing practices by national brand manufacturers in producing private label products that are still perceived by most consumers as lower price option to the national brands.

2. Literature review

Originally, private labels were positioned as alternative options to national brands that provide good value for money or low price. The low-price advantage has been the major selling point and therefore, private labels in themselves serve as cues to evoke perception of value

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(Zeithaml, 1988). In other words, a product can be perceived as low price simply because it carries a private label brand (PLB). Despite recent developments of private label brands being positioned as organic, premium, and "healthier" than they were once thought of, and are priced not cheaper than the leading national brands (NB) (Richardson, 1997; Tarnowski, 2005), the mainstream consumers seem to continue associating private label brands with cheaper version of the leading national brands. Research findings still demonstrate that, in general, consumers still perceive differences between private label brands and national brands on dimensions such as price, quality, value, perceived risk, and trust, even at subcategory level (Nenycz-Thiel and Romaniuk, 2009).

Perceived quality is defined as the “consumer's judgment about a product's overall excellence or superiority” (Zeithaml, 1988). With respect to perceived quality, when a consumer views a brand to be of better quality, the attitude toward that brand is expected to be higher. Numerous research suggest that there are significant differences with regards to perceived quality between private label brands and national brands, demonstrating that consumers place higher evaluation towards product quality of national brands than that of private label brands (Bellizzi et al., 1981; Hawes et al., 1982; Richardson et al., 1994). This is evident in the fact that the improvement of packaging design and product quality of store brand products in the UK contributed to the high market share of private label brands (Wells et al., 2007).

Private label brand buying has been greatly affected by a number of consumer factors such as perceived risk and attitude (Batra and Sinha, 2000; Dunn et al., 1986; Richardson et al., 1996). Some of the first studies examining the effect of brand on perceived risk always compare generic and national brands (Bearden and Mason, 1978; Reindenbach et al., 1983). All findings lead to a conclusion that generic brands are perceived to bear more risks national brands. Dunn et al. (1986) added store brands (or private label brands) into the comparison between generic and national brands and found that, while store brand was still perceived to be of better quality than generic brands, they were still seen as inferior and riskier than the national brands. Later research by Dick et al. (1995) and Richardson et al. (1996) also investigated the effect of brand on perceived risk by making comparison between store and national brands and produced similar findings. Some research dated back two decades ago found that, compared to national brands, consumers regarded private label brands as having highest risk on performance, but lowest risk on financial measures (Dunn et al., 1986). Decades later, research findings still showed that the consumers still expected private label brands to entitle lower quality than that of national brands (Dick et al., 1995; De Wulf et al., 2005; Cheng et al., 2007). Making a wrong purchase decision is an important risk factor as private label brands are seen by consumers as being inferior to national brands on aspects such as reliability, prestige, and quality attributes (Bellizzi et al., 1981). Thus, in the effort of reducing the risk factor, national brand is believed to provide a much safer choice in many purchasing and consumption situations (Baltas, 1997). In general, consumers still perceive national brand as superior in all aspects compared to the PLBs.

The production of private label brands may be contract manufactured by the national brand manufacturers, which utilize their excess production capacity to generate more revenues. Although it is an ordinary practice in the retail industry, contract manufacturing by national brand manufacturers has been hidden from the public. This is true as private-label production by national brand manufacturers is of great managerial interest but lacking empirical research, which can be attributed to the secrecy about the question of which national brand manufacturers produce private label brands (Sayman and Raju, 2007; Sethuraman, 2009; Sethurman and Raju, 2012; Braak et al., 2013). This secrecy may also be attributed to the national brands’ concern about their image, consumer perception and/or competitive advantage. The Internet serves as a media from which information on contract manufacturing is openly discussed and made available to the public. Exposure to such information may alter consumers' attitude towards both the private label brands and national brands.

Consumers are active individuals who process information in their decision-making process. Unfortunately, often times, consumers are faced with information asymmetry while the very basic ingredient for consumer decision making is information. Information asymmetry occurs when “different people know different things”, which suggests that the distribution of information is asymmetrical to the public (Stiglitz, 2002). A type of information that highlights the importance of asymmetry is information about quality. Asymmetrical information becomes critical when consumers are not aware of the characteristics of a certain brand (e.g. private label brand). Signaling theory reduces this information asymmetry between parties (Spence, 2002). In his previous study, Spence (1973) used labor market to model the signaling function of education. The lack of information that potential employers have on job candidates encourages employers to use education level as signals of quality of the job candidates; thus reducing the information asymmetry.

The analogy can be made in the context of contract manufacturing by national brands manufacturers to produce private label brands. The exposure of information on such manufacturing practice to the public will allow consumers to use it as a signal to determine the private label brand's quality. Thus, when consumers find out that a private label brand (perceived to be cheap and of low quality) is made by manufacturers of a national brand (perceived to be of better quality and higher price), drawing upon signaling theory, they may infer that the private label brand is not that different from the national brand in terms of quality or product performance as they both share the same manufacturing facility in the production process.

The signaling theory has been used extensively in marketing and consumer research (Kirmani and Rao, 2000). Consumers used certain indicators to evaluate unobserved quality of a product or service. Serving as signals to consumers, these indicators range from brand names to advertising expenditures. Brand names can be used to communicate unobserved quality because sellers of branded products are assumed to have invested heavily on advertising, packaging, and product design to build brand equity (Erdem and Swait, 1998). Some correlational studies also confirm that product quality is affected by brand names (Erdem and Swait, 1998), providing general support for signaling predictions in the case of low-priced consumer goods (Rotfeld and Rotzoll, 1976).

Therefore, we propose the following hypotheses:

H1. Contract manufacturing information exposure has significant effect on consumers' perceived quality toward the private label brand; in that when consumers know that a private label brand is manufactured by a national brand manufacturer, their perception of the private label's quality would be higher than when they do not know.

H2. Contract manufacturing information exposure has significant effect on consumers' perceived risk toward the private label brand; in that consumers' perceived risk toward private label brand is lower when the consumers know that a private label brand is manufactured by a national brand manufacturer than when the consumers do not know.

It seems to be a common sense that when a consumer perceives a brand to be risky, their likelihood to purchase the brand would decrease. Most previous studies supported the notion and concluded that perceived risk had a negative effect on attitude, that is, the higher the perceived risk of private label brands, the lower the attitude toward the private label brands. The greater the perceived risk associated with private label brands, the lower the consumer likelihood to buy the private label brands (Erdem et al., 2004; Richardson et al., 1996). Consumers will not prefer private label brands if the level of perceived risk toward private label brands is high, and thus, they will turn to national brands as less risky choice (Narasimhan and Wilcox, 1998). National brands are perceived as less risky because as a result of large advertising campaigns, national brands have developed strong brand