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Strategic Interactions in Franchise Relationships

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5 The DA system

Section 1 introduces the SCTs for DA, while sections 2 to 5 discuss the development of the franchise partners' perceptions of the independent variables. The indicators used for these variables are summarized in Appendix 2. Section 6 discusses the responses that franchise partners generally adopted toward each other during both SCTs. Section 7 then takes a closer look at individual franchise relationships by analyzing which independent variables influenced the franchise partners' adoption of responses. Finally, section 8 presents the three types of conclusion (see section 4.3.5) based on the DA system and its SCTs.

The abbreviations used in this chapter are explained in Appendix 11.

5.1 Historical sketch of DA and an introduction to its SCTs

5.1.1 Historical sketch of DA

In 1942, five independent Dutch druggists started a cooperative called 'Dienende Actie' (DA), which can be translated as 'Serving Action'. They were dissatisfied with the turnover of their businesses and the performance of their suppliers, and decided to form a mutual support network so that all the partners would share the benefits if, for example, one partner was able to buy in a product at a low price. In the early years, the DA druggists focused on joint purchasing and the use of the DA name on their stores. In 1947, the name *Dienende Actie* was changed to *Drogisten Associatie* (Druggists' Association). In the years that followed, the DA group expanded rapidly and broadened the scope of its activities. By 1950, the number of druggists participating in the DA system had increased to 150. It increased further to 500 in 1960 and to 1,000 by 1982.

Gradually, the Board of the Druggists' Association sensed an increasing need for closer co-operation, with additional requirements and requirements for the DA franchisees, in order to face the increasing competition from discount drugstores and supermarkets. An important step in terms of purchasing activities was DA's acquisition, in 1989, of a majority shareholding (80%) in the wholesale organization Tendo Haco Farmacie BV. As a result of this acquisition, the Druggists' Association became a purchasing organization with its own wholesale operation through which the DA franchisees were required to purchase their goods. In 1990, the Druggists' Association became the 100% owner of Tendo-Haco.

A further development was the launch, in 1989, of the STIP system, an alternative to DA for franchisees who were unable or unwilling to meet the increasing requirements of DA. These druggists often owned stores in villages or suburbs. From that date, members of the Druggists' Association could operate either under the DA name or the STIP name. The STIP system will be dealt with separately in this study, and is discussed in Chapter 6.

In 1991, the Druggists' Association adopted an even more structured and centralized approach to its commercial activities by cooperating with the wholesale organization Interpharm BV²². This was done because the wholesaler Tendo-Haco had performed very badly and was dissolved. The Druggists' Association and Interpharm entered into two joint ventures: Dynadro BV and Dynaretail BV (see Appendix 10). Dynadro would handle

²² Interpharm BV was in turn a 100% subsidiary of Internatio Müller (this organization also played a role in SCT7 of this study, see Chapter 8)

wholesale drugstore activities, while Dynaretail would handle retailing and other support activities for the druggists²³.

Before the cooperative was formed, the Druggists' Association administered two drugstore systems (DA and STIP). Interpharm also had two drugstore systems (Eurodrogist and WPP). This resulted in four drugstore systems to be managed by Dynaretail. Shortly after Dynaretail started up, management decided to merge Eurodrogist with DA, and WPP with STIP. In 1994, an additional drugstore system known as DA D'Attance was launched for the luxury segment of the market. Eventually, this resulted in three drugstore systems for Dynaretail: DA, STIP and DA D'Attance.

In December 2000, Dynaretail and Dynadro merged, resulting in a new organization with the same name as the former wholesaler: Dynadro BV. The new Dynadro was responsible for marketing *and* wholesaling activities for DA, STIP and DA D'Attance. The new Dynadro had two shareholders, each owning 50% of the stock: the Druggists' Association and Alliance UniChem²⁴. In January 2002, the Druggists' Association purchased the Alliance Unichem interest and became the 100% owner of Dynadro. Fig. 5.1 shows the structure in terms of the different levels of franchising (see Fig. 1.2). The broken line around DA is printed in bold because this chapter focuses on the DA system.

Druggists are members of the Druggists' Association

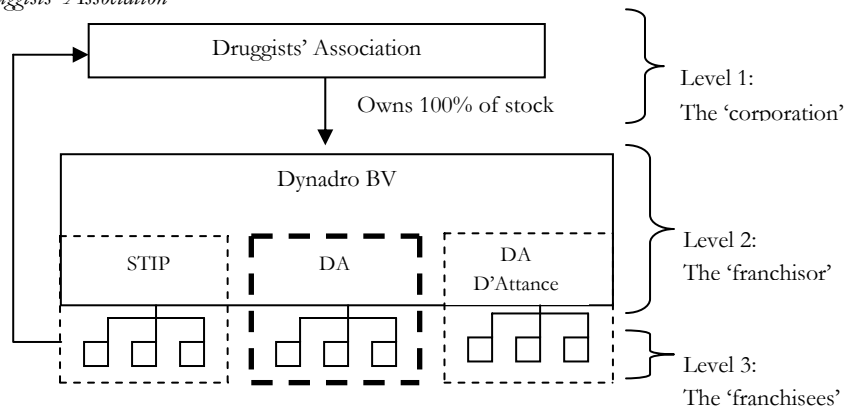


Fig. 5.1: The DA system from January 2002 to January 2004

For DA, this chapter will focus on two strategic change trajectories (SCTs). SCT1 focuses on the changes at DA when Dynaretail was started in 1991. In short, management wanted DA to operate more like a franchise system with a more or less standardized business format (SCT1: *'Toward business-format thinking'*, see section 5.1.2). In the remainder of this chapter, management during SCT1 is referred to as management1. SCT2 started in 2003 when a new management team was installed at the new Dynadro (management2). Management2 introduced three changes: 1) integration of DA, STIP and DA D'Attance into a single DA system with a new commercial policy; 2) the signing of a standard

²³ This chapter mainly focuses on Dynaretail and its management because Dynaretail took over all retailing and supporting activities, including the management of the DA system.

²⁴ Alliance Unichem was a British pharmaceutical organization that had taken over Interpharm from Internatio Müller

franchise contract by all DA franchisees; and 3) the introduction of a new corporate governance structure for the new Dynadro BV (SCT 2: *'Integration and renegotiation'*, see section 5.1.3).

The developments in the DA system and its central organization are summarized in a general time line in Fig. 5.2.

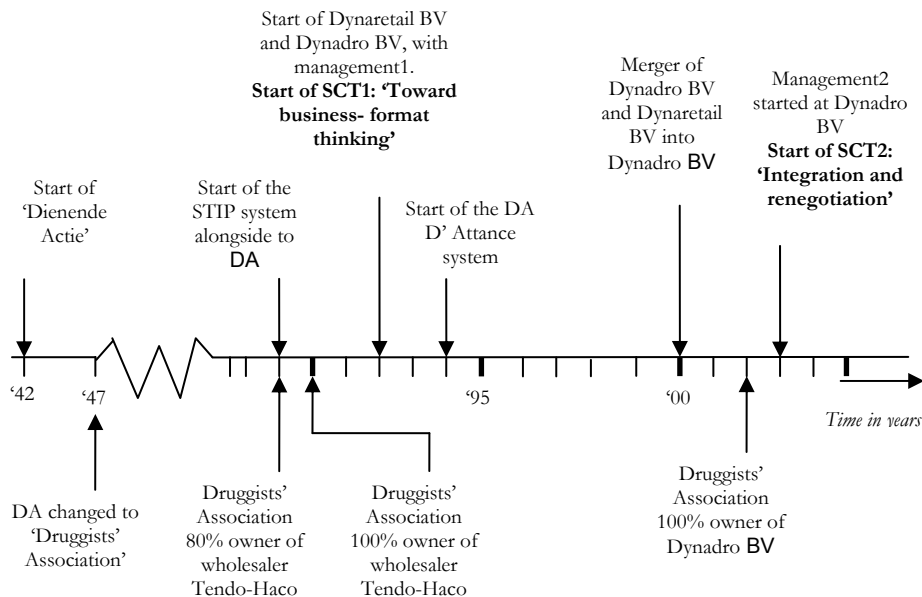


Fig. 5.2: General time line for the DA system and the Druggists' Association

5.1.2 Introduction to SCT1: 'Toward business-format thinking'

Dynaretail's objectives were set down in a business plan. The main objective was to offer druggists professional support in the form of different franchised drugstore systems, each of which would have different business formats²⁵ and focus on different segments of the market. The use of a business format meant that management1 wanted the druggists participating within the different systems to operate under the same name with a uniform identity for customers, and standardized back-office processes (e.g. purchasing and automation).

SCT1 is the introduction of the business-format approach at DA. However, management1 also wanted to introduce this in Dynaretail's other drugstore systems. Before SCT1, the DA system was loosely organized and individual DA stores were very different from each other, ranging from small- village stores and medium-sized stores in towns, to large luxury stores in city centers. Management1 aimed to develop different systems and business formats for each type of store. As mentioned previously, STIP was launched in 1989 for smaller DA franchisees who could not fulfill the increased DA requirements.

²⁵ For the definition of 'business format' in this study, see Chapter 1.

With the 'reanimation' of STIP (SCT3, see 6.1.2), management1 hoped to convince DA franchisees with smaller stores to switch to STIP. Similarly, it attempted to convince franchisees with larger luxury stores to switch to DA D'Attance, which was launched in 1994. Management1 thus aimed to make each system more homogeneous in terms of stores, resulting in a structured, standardized approach, which would make it easier to increase the degree of hardness and thereby the degree of uniformity toward customers.

Management1 had three main reasons for implementing SCT1:

- Motives related to competition. According to management1, the most important threat to independent druggists was the rise of competing – mostly discount – drugstore systems, such as Kruidvat, ETOS and Schlecker. These usually consisted of company-owned units, and had a uniform identity for customers. The market share of these systems had grown steadily over time, while the market share of independent druggists had declined. Additionally, other organizations – such as supermarkets and pharmacists – had increased the share of drugstore products in their assortments. Management1 predicted an even greater increase in chain stores and, if no action was taken, the disappearance of 'completely independent druggists' (CIDs) followed by the disappearance of DA franchisees. Therefore, it thought the DA- franchisees needed to increase the level and scope of their cooperation.
- Motives related to customers. Consumer research showed that DA mainly attracted customers older than 35 years and customers with middle and higher incomes. Therefore, management1 aimed to reach a broader target group. Additionally, research showed that DA stores had a strong position in assortments for which advice was important (e.g. health and luxury cosmetics), but had a weak position in terms of price image. Management1 considered this a serious threat due to the rise of the discounters, and it aimed to adapt the price image of DA.
- Motives related to suppliers. A distinction can be made between suppliers of 'regular' drugstore products ('regular suppliers') and suppliers of luxury products, such as Lancôme, Chanel and Dior ('luxury suppliers'). In order to negotiate with the regular suppliers, it was important for Dynaretail to have one or more franchisee-like systems with a large number of franchisees who could sell the supplier's products. With a large number of franchisees obliged to sell the supplier's products, management1 aimed to realize economies of scale in purchasing. Additionally, the regular suppliers could help in supporting promotional activities, for example by contributing to the cost of advertising. For the luxury suppliers, management1 argued that the latter increasingly attached importance to a strong market position of the DA franchisees, and management1 thought that only a recognizable system with a uniform quality level could meet the requirements of luxury suppliers.

Management1 achieved only some of its goals for SCT1. Over a period of ten years, it created three different franchise-like systems: DA, STIP and DA D'Attance. However, the DA system was still not very uniform and management1 had not succeeded in introducing a franchise contract. As already pointed out, the retail organization Dynaretail and the wholesaler Dynadro merged into a new organization called Dynadro in 2000. In 2003, management2 took over the management of the new Dynadro organization and implemented SCT2: 'Integration and renegotiation'.

5.1.3 Introduction to SCT2: 'Integration and renegotiation'

Management2 still perceived fierce competition from other drugstore systems, and it wanted to strengthen the DA brand name. It also thought DA was still perceived to be too expensive and needed a more uniform and distinctive positioning. Management2 aimed to improve the performance of Dynadro and its drugstore systems by introducing the following changes:

- The merger of DA, STIP and DA D'Attance into a single DA system with a new business plan. Research had shown that the DA system was well known among consumers, but they were not very familiar with STIP and DA D'Attance. In order to benefit from the well-known DA name and improve the stores' position in the market, management2 thought these systems should be brought together in a single new DA system. Within this new system there would be three categories or store 'formats' corresponding to the earlier systems STIP, DA and DA D'Attance. 'DA Basic' corresponded to the former STIP, 'DA Core' was the former DA, and 'DA Beauté' corresponded to the former DA D'Attance²⁶.
- The introduction of a standardized contract (FSO²⁷) between Dynadro and all its druggists. This had been a subject of discussion between management1 and DA franchisees for several years. The only thing the DA franchisees had in common was their membership of the Druggists' Association²⁸ and the use of the DA name on their stores. Dynadro already had a very simple franchise-like contract with some of the druggists, those who had joined DA in the late 1990s, but this was a relatively small group. Additionally, there were many different contracts between the former wholesaler Dynadro and the various druggists. Overall, there was no standardized contract specifying the rights and requirements of both franchise partners. Management2 thought that such a contract was necessary for the new DA system in order to improve its decisiveness.
- The introduction of a new corporate-governance structure to speed up decision-making processes and to improve the transparency of these processes within Dynadro itself and toward its druggists. In previous years, many committees and working groups of DA druggists had been involved in decision-making. In June 2003, a new structure was introduced: one management team for Dynadro, a Supervisory Board and a Council of Drugstore Owners, each with different tasks and rights (see 5.2.4). The new structure was set down in the new Articles of the Druggists' Association that came into force on June 17, 2003.

5.2 Strategic compatibility

This section will discuss the strategic compatibility between the franchise partners in terms of the characteristics of the five franchise systems. Each subsection consists of the following parts: *What the franchisor wanted*, *What franchisees wanted* and *What actually happened*.

²⁶ The names 'DA basic' and 'DA core' were used only by management2 to distinguish between the store types. Consumers were not aware of these names. The name 'DA Beauté' was presented to consumers so that they knew that these were luxury DA stores.

²⁷ FSO stands for the Dutch terms 'Formule Samenwerkings Overeenkomst'

²⁸ The Articles of the Druggists' Association applied to this membership.

5.2.1 Strategic compatibility regarding positioning during SCT1

What the franchisor wanted

According to management1, the DA stores were generally positioned in the medium to high end of the market in the early 1990s. The discounters served the lower market segments with wide product ranges and low prices. ETOS served the middle segment with a balanced assortment of health, care and some cosmetics, including luxury cosmetics, while the higher segments consisted of Bijenkorf, Douglas, local perfumeries (highest segment) and 'traditional' drugstores (high to medium). The DA stores were comparable to the traditional drugstores with a high added value due to their specialized assortments and high standards of service. Management1 aimed to position DA more in the middle segment of the market by adapting the assortment, price level, promotional activities, and appearance of the stores.

In the first place, management1 thought DA's assortment was too specialized and had too many products with high margins. Over time, DA franchisees had replaced some low-margin product groups, such as diapers and baby food, with product groups with higher margins, such as perfumes²⁹. Management1 wanted to reintroduce the lower-margin products so that they could serve as 'traffic-builders'. These products were presented in promotional brochures and television advertisements, and were expected to attract more customers. The traffic-builders included the product groups that were reintroduced, and product groups that were not directly or not at all related to basic drugstore ranges. This study distinguishes between 'non-drugstore-related products' and 'drugstore-related products'³⁰. 'Non-drugstore-related products' (in Dutch: *branchevreemd*) are completely unrelated to the traditional drugstore assortment, such as CDs, t-shirts and vases. 'Drugstore-related' (in Dutch: *brancheverwant*) refers to products that are somehow related to traditional drugstore ranges, such as hair accessories or toys.

Second, management1 did not really want to modify the DA system's service level. Market research showed that consumers appreciated the professional advice and services offered in DA stores. Management1 intended to keep this service level, while broadening DA's target market.

Third, in order to reach a broader target group, management1 aimed to change DA's high-price image. Different types of promotional activities were used to achieve this. From 1996, promotional activities for DA were organized via the national media. They were realized in cooperation with certain suppliers, which meant that the suppliers contributed to the high cost of the promotional activities. In return, management1 promised these suppliers that their products would be prominently displayed in every DA store. The promotional products were sent automatically to the druggists, thereby increasing the degree of hardness of the DA system (see section 5.2.2).

Finally, management2 aimed to change the appearance of the DA stores. The stores often had a relatively luxurious interior, which gave customers the impression that their products were expensive. Management1 wanted a new look for the stores, for example with tiled floors instead of luxury carpeting.

²⁹ This was not specific to DA franchisees. Other drugstores and drugstore systems – such as ETOS – had also dispensed with low-margin product groups due to competition from supermarkets and discount drugstores.

³⁰ In practice, these terms were often used interchangeably.

What franchisees wanted

With respect to the positioning of DA, there were two changes that the majority of DA franchisees disagreed with:

- The introduction of low-margin products and non-drugstore-related products. They disagreed with this for two reasons. First, they perceived these products as costly because they resulted in high quantities of ‘remnants’ that the franchisees could not sell. According to one franchisee: *‘We had to purchase a certain quantity of these products (or they were supplied automatically, EC). These were often very bizarre products, such as bike lamps. When you’re left with these products, you might as well just throw them away or put them in the attic. These products required a lot of investment, which you could not then put into your regular drugstore assortments’* Second, DA franchisees thought that the non-drugstore-related products did not fit in with their drugstores and the druggists’ expertise. One franchisee put it like this: *‘I hate the non-drugstore-related products. They take up space. Some are a success, others aren’t. I don’t know anything about these products. When a customer asks: “Does this t-shirt fit me?” I have no idea; I know absolutely nothing about these products.’*
- The store appearance was another important issue. According to one franchisee who was involved in one of the ‘Boards of Participants’ during SCT1 (see section 5.2.4): *‘The DA-druggist is the lady with the pearls and tidy hair, dressed in a skirt and jacket – I’m exaggerating a bit – and she sees the drugstore as a part of herself. And that is why customers come to her store. She wants to create a pleasant atmosphere in her store, but she forgets that her store is not her home. The carpeting on the floor simply intimidates the customers. She doesn’t realize that the feeling she is putting into her store is enough. In a neutral environment you have a store that is accessible to everyone.’* In addition, the new-style store required a financial investment that many franchisees were not willing to make.

What actually happened

Management’s desired changes in positioning occurred very slowly. This is illustrated by the results of research performed by GfK, a market research agency that carries out yearly consumer surveys for the five largest Dutch drugstore systems (Kruidvat, DA, ETOS, Trekpleister and Schlecker). For several years, DA scored highest on friendliness, expertise and service, but it had the lowest score for price level and the attractiveness of its promotions.

The slow changes in positioning can be explained by the fact that the majority of DA franchisees did not agree with the changes, and were reluctant to change. Moreover, management1 did not strictly enforce the changes, although the DA Articles of Association made provision for this (see 5.2.2).

5.2.2 Strategic compatibility regarding positioning during SCT2

What the franchisor wanted

A new business format (DA 2005) with a new commercial policy had been developed for the new DA system in the years before SCT2³¹. Management2 focused on changes in the assortment, price level, promotional activities, and store appearance.

In terms of assortment, emphasis was placed on health and beauty. However, according to management2, the DA assortment should also include regular drugstore products,

³¹ Management1 had already started developing the DA-2005 business format and management2 further refined it.

drugstore-related products, and non-drugstore-related products. With regard to the regular drugstore products in particular, management wanted to introduce competitive pricing. In addition, management still thought that the assortments of several DA franchisees were too specialized.

With regard to price level, management thought that DA still had an expensive image, which intimidated customers. For many years, the GfK research results had shown that DA scored very highly with customers on aspects such as professional advice and friendliness of staff. However, DA had the most expensive image of all the drugstore systems in the GfK research sample. Therefore, in 2003, management introduced 'Vast Laag' ('Always Low') campaigns in 2003 (later 'Da's laag!', 'DA's Low!'). Fixed low prices were introduced on certain products in order to improve DA's price image.

Management wanted to change the appearance of DA stores. Although management had already tried to convince the franchisees that this was necessary, some DA stores still had pre-1990 interiors. Therefore, management aimed to introduce the DA 2005 concept, which would give each store a 'fresh' and not-too-expensive look. Additionally, a new DA logo was designed to give the stores a more modern image.

The actual implementation of DA 2005 depended on the format: DA Basic, DA Core or DA Beauté. This chapter will focus on DA Core because most DA franchisees were supposed to switch to this during SCT. Chapter 6 will focus on the changes made by STIP-franchisees to the DA Basic format. The basic differences between these formats related to assortment and store appearance. The DA Basic stores could complement their drugstore assortments with a relatively large number of non-drugstore-related goods such as postcards, magazines and toys. DA Beauté stores were supposed to have a large range of luxury products and some non-drugstore-related products, in addition to the regular drugstore products. DA Core was between DA Basic and DA Beauté: the stores sold regular drugstore ranges with non-drugstore-related products and a number of luxury products.

What franchisees wanted

The majority of DA franchisees agreed with the changes in positioning. In particular, the Vast Laag ('Always Low') promotions played an important role in the franchisees' perception of strategic compatibility on positioning. The DA franchisees mostly agreed with the idea of the Vast Laag promotional activities, but several of them had problems with the purchase price of Vast Laag goods. They thought that Dynadro should lower the purchase prices so that the druggists would still have some margin on the Vast Laag products. Moreover, because certain goods were to be supplied automatically, they were afraid that the quantities supplied would be too high (see also 5.2.2).

What actually happened

As mentioned above, GfK research had shown for many years that DA was the best drugstore system in terms of advice, range, quality, etc., but it still had an expensive image. The GfK results for 2003 showed that DA still scored lowest for price compared to other drugstore systems but, on the other hand, the DA score for prices had improved over the years.

The adoption of the new store exterior was delayed for several months due to problems with the supplier of the illuminated signs with the new DA logo.

Fig. 5.3 presents the timeline for DA's positioning and distinguishes between DA Basic, DA Core and DA Beauté, which were all supposed to have a slightly different positioning.

Only the timeline for the desired scores of DA Core franchisees is shown, because this chapter focuses on DA and DA Core.

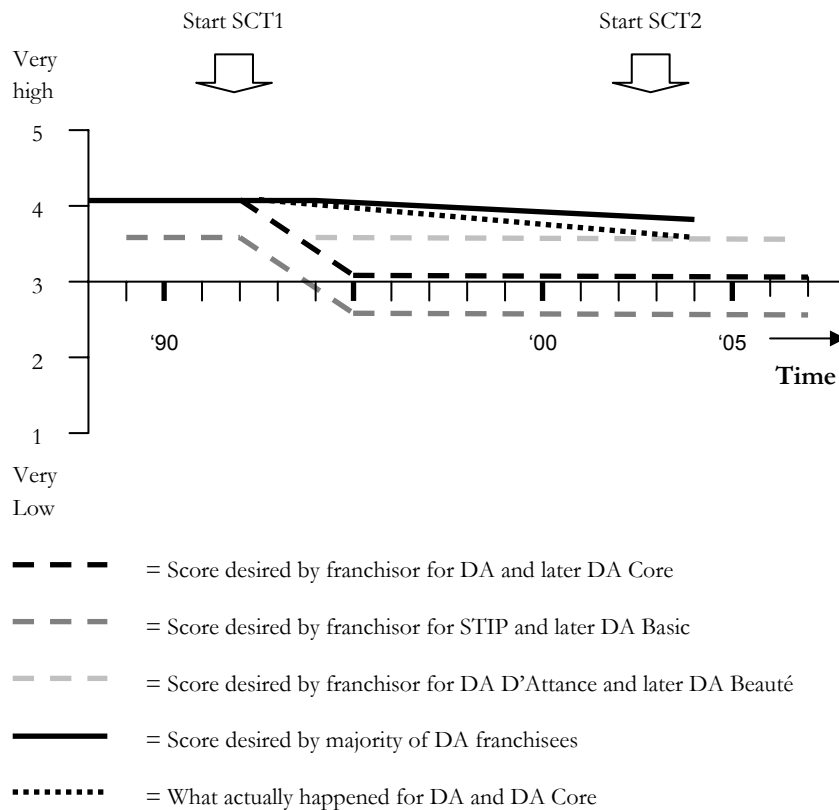


Fig. 5.3: Timeline for positioning

5.2.3 Strategic compatibility regarding degree of hardness during SCT1

What the franchisor wanted

Management1 thought the image of DA stores was not uniform enough for customers. For several decades, the use of the DA name on the store exterior had been the only common feature of the DA stores, although the Articles of Association had always included provisions for imposing requirements with respect to business-format elements (cf. clauses 11 and 12 from the Regulations³²). Management1 aimed to create more a uniform appearance for DA stores by means of the following requirements:

- The collective promotional activities oriented to the traffic-builders were the most important requirements during SCT1. The aim of these products (drugstore-related and non-drugstore-related) was to attract customers to the stores. From 1996,

³² The Articles of Association consisted of the Articles themselves and a set of Regulations. References to the Articles of Association include the Regulations, or indicated otherwise.

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management1 launched major television advertising campaigns. These were organized in cooperation with suppliers, who made a significant contribution to the cost. DA was an interesting partner for these suppliers because it had many drugstores that could sell their products. The suppliers expected that the DA franchisees would display their products in a prominent position in the stores. Therefore, the products were supplied automatically, and the franchisees were instructed where to place the products in the stores.

- Management1 tried to introduce 'shelf-designs' in which the composition of part of the store's range was prescribed. The shelf designs were developed in cooperation with suppliers. Because of the large number of franchisees in the group, management1 could give the suppliers guarantees that they would purchase a certain quantity of goods. The guarantees were intended to secure attractive purchase prices for these goods.
- Management1 wanted each store to meet certain criteria in order to present a uniform image and to reposition DA lower in the market. As mentioned above, one important example was the switch from carpets to tiled flooring in the stores. Management1 wanted all the franchisees to implement this change.

In addition to requirements for business-format elements, management1 tried to convince the druggists to purchase their products from Dynadro. The Articles of Association included provisions for requiring franchisees to purchase via the Druggists' Association's wholesaler Dynadro. At the time, several druggists were purchasing their goods from other wholesalers, and management1 wanted to prevent this. Additionally, management1 tried to convince the druggists to adopt a single automation system.

The Articles of Association of DA already included provisions for imposing requirements designed to 'protect' the DA system. One example was clause 7j, which stated that DA franchisees were not allowed to participate in the activities of other market parties in the drugstore industry.

With respect to the degree of enforcement, it is striking that several requirements for DA franchisees were already mentioned in the Articles of Association. There were already several provisions for establishing requirements for DA franchisees, such as minimum floor areas, the store interior, store exterior, product assortments, promotional activities, and minimum purchase quantities. However, these Regulations were never strictly enforced, and when management1 tried to convince the franchisees that several of the requirements were necessary, several franchisees resisted.

What franchisees wanted

A large group of franchisees disagreed with the requirements, particularly those relating to non-drugstore-related goods. These goods posed the greatest problems because they were supplied automatically. Several DA franchisees did not comply with the agreements that management1 had made with the suppliers. They did not position the products in their stores according to the suppliers' wishes, and this undermined Dynaretail's negotiating position with its suppliers.

The CEO twice experienced a situation in which franchisees did not comply with agreements made between the management and suppliers. At that point, management almost decided to discontinue these activities because it damaged DA's reputation vis-à-vis the suppliers. The CEO explained: *'Then there was disagreement. One group thought that these*

activities should be continued, while another group thought that they should not, because they perceived them as too restrictive. The druggists who thought we should continue said that we had to convince the others to participate. But we thought we had done enough... We said that we thought it was their problem. And then we reached an important step in the group process because the "good" started convincing the "bad" saying that if they did not want to participate that they should leave the DA system... They came back to us to say that they had convinced each other to continue with the promotional activities. And I said: 'I'm glad you've worked it out, but we will continue on one condition, and that is a mystery tour'³³. I will not take the risk of you failing to keep to the agreements again, and damaging our reputation.'"

With respect to other changes (shelf design, store appearance), several druggists disagreed and simply did not carry out the changes.

What actually happened

As mentioned above, the only requirements that were actually enforced by management1 were the promotional activities and automatic supply of certain goods. The products were supplied automatically, so the franchisees had little choice. Management1 tried to convince the DA franchisees to participate in the other changes, but it did not dare to enforce them because it was afraid that many DA franchisees, who were a very important source of income for the franchisor, would then leave the organization. Therefore, the DA system was softer than management1 actually wanted it to be.

5.2.4 Strategic compatibility regarding degree of hardness during SCT2

What the franchisor wanted

Management2 wanted the DA franchisees to sign the FSO and adopt the DA 2005 business format within a certain time period. The FSO established the rights and requirements of Dynadro and the franchisees in more detail than the previous Articles of Association. The FSO had an important supplement: the format handbook, which focused on the implementation of DA 2005.

With regard to compulsory business format elements, management2 wanted to apply an '80-20 rule', i.e. 80% of the elements should be standardized, while franchisees would have about 20% scope to make local adaptations. The most important requirements were:

- The DA franchisees had to fulfill certain minimum requirements: sell DA's own-brand products, offer a certain basic range, and sell the products promoted in offer brochures, which were often supplied automatically. Management2 was aware that the automatically supplied products had caused problems with franchisees in the past, and it had developed another formula for calculating the quantities to be sent to each franchisee. The drugstores were divided into turnover categories, and a quantity was determined for each category.
- Management2 aimed to increase collective promotional activities. For the DA franchisees, this did not really change because they were accustomed to sending out brochures every two weeks. This mostly affected STIP-franchisees who were supposed to switch to the DA Basic format (see Chapter 6).
- Management2 wanted all stores to change to the new DA-2005 store design. The handbook specified the store appearance for each format. The investment

³³ A 'mystery tour' means that by order of Dynaretail an anonymous customer could visit a store unexpectedly to check whether the franchisee has adopted certain requirements.

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requirements for DA Basic stores were lower than for DA Core and DA Beauté stores. For each format, management wanted to give franchisees some freedom of choice with respect to the store interior. DA Core stores could choose between two types of tiled flooring and two types of laminate, while carpet was no longer allowed.

With respect to compulsory services, the most important requirements were as follows (as stated in the FSO):

- DA franchisees had to purchase at least 75% of their range from Dynadro.
- Management² wanted to introduce a compulsory automation system for all DA franchisees within a certain period of time (approx. 18 months). Franchisees could choose between two systems offered by a supplier, with Dynadro acting as the intermediary.
- The FSO stated that management could oblige franchisees to participate in training. According to the CEO, several franchisees were still focusing on their specialist knowledge as druggists, while they also needed to increase their managerial knowledge.
- The FSO required franchisees to provide certain information about their store, such as turnover levels and profit and loss accounts. Management² thought it could use this information to make better decisions for the DA system.

Some of the contractual clauses in the FSO resulted in heated discussions between management² and the franchisees. These clauses dealt mainly with the protection of the DA brand and system.

- The ‘Continuation/Family clause’ (clause 26). This clause stated that, if a DA franchisee died or wanted someone else to take over the store, the candidates would have to meet certain criteria and sign the FSO. This meant that family members could no longer simply take over the business.
- The ‘Competition clause’ (clause 9) specified that, if the franchisee should illegally end the FSO before its term expired, he would not be allowed to undertake activities similar to those of DA franchisees and Dynadro in the same town for a period of one year after the termination of the relationship.
- The ‘Selling clause’ (clause 27) stated that a franchisee who wanted to sell his or her store would first have to offer the store to Dynadro for a price comparable to the market price. Dynadro would then try to find another franchisee to buy the store. If Dynadro would not succeed in finding a buyer, the franchisee would be allowed to sell the store to a third party. This clause was designed to protect Dynadro’s locations and prevent competitors from acquiring its stores.

Management² intended to increase the level of enforcement in order to create a more uniform identity for DA. There were two means by which management² would do this. First, it wanted managers from Dynadro to visit the stores more frequently in order to help franchisees with promotional activities and other requirements, so that these could be carried out more effectively. Second, the FSO contained a ‘Penalty clause’ (clause 31) specifying that DA franchisees who, deliberately or otherwise, did not comply with the contract, would be required to pay a fine. There were different fines for different infringements, varying from EUR 5,000 for minor infringements (e.g. not using

promotional materials in the store) to EUR 40,000 for major infringements (e.g. not participating in group promotions).

What franchisees wanted

With respect to the business format elements, DA franchisees still perceived most problems as rooted in the automatic supply of certain goods. These could be drugstore goods, drugstore-related goods or non-drugstore-related goods, all of which required investment. Moreover, for several franchisees, this was not merely a financial issue but an issue relating to their independence. Because the goods were supplied automatically, they no longer felt that they were independent business owners.

Several franchisees were hesitant to invest in the new DA-2005 format due to the high costs involved. By way of a compromise, the FSO stipulated that franchisees could choose their own contractor to make the interior alterations.

Another requirement that several franchisees considered problematic was the requirement to purchase at least 75% of their range from Dynadro. The franchisees thought that the wholesaler's prices were too high, and therefore did not want to be obliged to purchase from Dynadro.

Several other clauses in the FSO brought reactions from franchisees, namely the Continuation/Family clause, the Selling clause, and the Penalty clause. The Continuation/Family clause in particular brought several emotional reactions from DA franchisees, many of whom felt that it was unfair that their children might not be able to take over the business they had worked so long to build. As one franchisee put it: 'If my daughter can't take over my business, I'd rather burn it down.' The Selling and Penalty clauses did not result in such strong emotional reactions, since the consequences for franchisees would be largely financial.

What actually happened

It is difficult to determine whether the degree of hardness actually increased after the introduction of SCT2 because data collection for SCT2 continued until March 2004 (when SCT2 was still ongoing). Nevertheless, during this process, the franchisees' deadline for signing the FSO was postponed several times over several months.

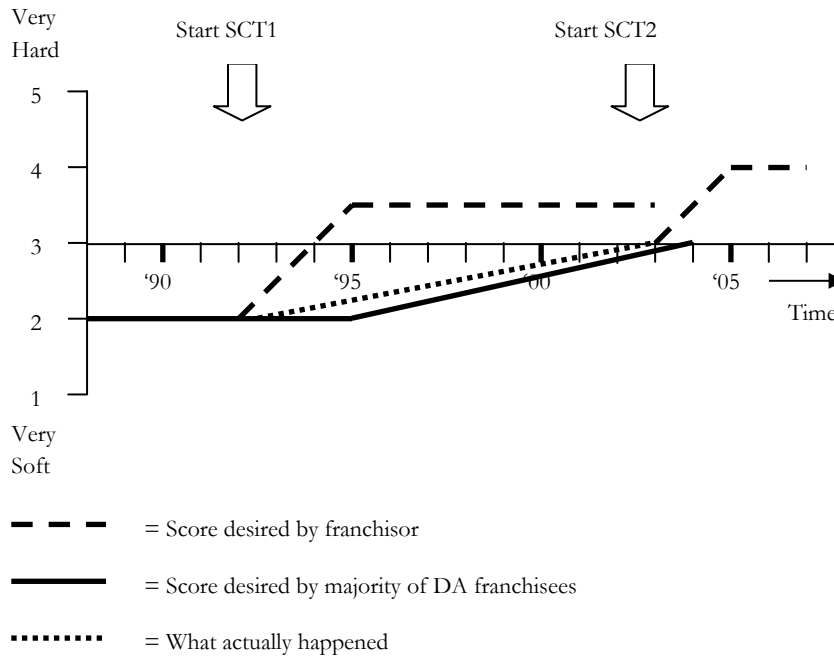


Fig. 5.4: Timeline for degree of hardness

5.2.5 Strategic compatibility regarding rate of innovation during SCT1

What the franchisor wanted

The research model distinguishes three levels of innovation: new products, new product groups and other adaptations to the business format, and the business format as a whole. Management1 wanted to increase DA's rate of innovation on all levels. According to management1, DA was particularly slow to innovate on the level of product groups and business-format adaptations and the business format as a whole. According to management1, DA franchisees remained focused on their old, traditional assortments and were reluctant to experiment with new product groups or new forms of service. Consumer research had shown that customers often regarded the DA stores as 'dusty' and 'not moving with the times'. According to management1, new products and product groups would attract more customers to the stores.

Moreover, management1 thought that the store appearance (as part of the business format) should be altered every six to seven years. Some store designs dated back to the 1970s. A manager of management1 said: 'If I had to call the shots, DA would have had a completely new logo in 1993. But you have to be careful not to alienate the druggists who think the changes are too fast and too radical. I had already developed a pilot store with a new logo, but then my boss (the CEO of management1, EC) said: "You can't do that; it won't work."'

What franchisees wanted

On the level of new products, DA franchisees agreed to a certain rate of innovation, albeit with limitations due to the level of risk involved. Since the level of risk remained within certain boundaries, this did not really pose problems for the relationship. However, several

DA franchisees regarded non-drugstore-related products as high risk. As one druggist put it: *'We've always been trend-followers rather than trendsetters. When you're a trendsetter, you risk being left with a lot of unsold products because, out of ten products, there's probably only one that sells well. We don't always have to reinvent the wheel.'*

As far as changes to business-format elements were concerned, the majority of DA franchisees were more cautious because these required greater investment and were considered riskier.

What actually happened

DA's innovation rate remained low over time because most franchisees were very cautious. Management1 did not really enforce the requirements, except in the case of certain new products that were supplied automatically. The rate of innovation varied widely between DA stores, particularly with regard to new product groups and business formats. This was because some franchisees adopted certain innovations while others did not.

5.2.6 Strategic compatibility regarding rate of innovation during SCT2

What the franchisor wanted

Management2 thought DA's rate of innovation was still too low, especially with regard to business-format changes and the business format as a whole. According to the CEO of management2: *'We are experimenting more now, but at the moment we're followers, and we follow Kruidvat, ETOS, Douglas and Ici Paris.... We also want to explore the possibilities for special introductions, with products that are not normally found in a drugstore range. We will try to set ourselves apart from the competition. For example, if you sell luxury cosmetics you might want to add make-up bags, blushers etc. ... We aim to do the same thing with our health range. In the past seven years we have opened fourteen combination pharmacy/druggists. We now want to speed up the sale of prescription drugs. So here we are also extending our boundaries.'*

In summary, management2 wanted the rate of innovation to increase on various levels. Moreover, it had a broader definition of 'new': it aimed at alterations that would be new not only to the DA system, but also to the drugstore industry as a whole.

Another important issue during SCT2 was the possibility of self-service for customers. A change in laws relating to non-prescription drugs made it possible for druggists to offer self-service. From July 2003, customers were allowed to take the medicines from the shelves. Management2 wanted all DA franchisees to offer this facility because DA should not lag behind this general development in the drugstore industry.

What franchisees wanted

The majority of DA franchisees were still cautious about innovation. On the level of new products, they were less hesitant, but often still reluctant to introduce new products because of the perceived risk.

On the level of new product groups and other business-format adaptations and the business format as a whole, the franchisees were more cautious because these required greater investment and involved more risk.

What actually happened

It is difficult to determine whether the rate of innovation actually increased during SCT2 because SCT2 was at a relatively early stage.

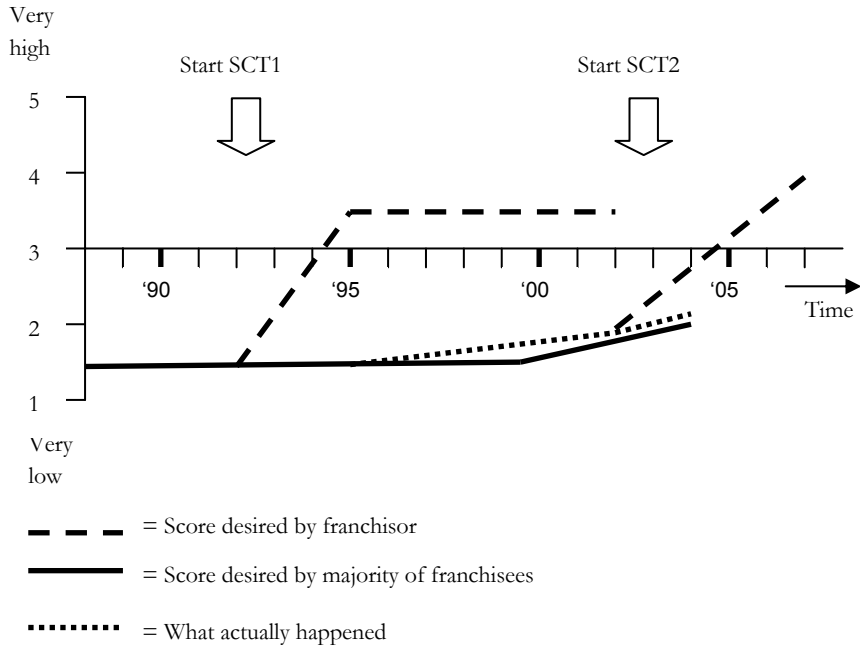


Fig. 5.5 Timeline for rate of innovation

5.2.7 Strategic compatibility regarding the organization of franchisees' strategic participation during SCT1

What the franchisor wanted

Before SCT1 and the launch of Dynaretail/Dynadro, the Druggists' Association had its own structure with several boards, committees and forty-one regional groups. Each druggist was part of a regional group. According to a manager, the topics discussed at the meetings of these groups were more operational than strategic, for example: sharing the benefits of bargains. He said: *'They mainly discussed bargains, such as "I've bought 48 pairs of clogs, who else wants to buy some"'. Then everyone had a drink and went home. It was sociable, and relationships became closer. Sometimes, suppliers would arrange an expenses-paid trip. One member from each regional group served on the Board of Representatives, which was supposed to discuss DA policy with the Board of the Druggists' Association. But the DA Board had usually decided everything already.'*

During SCT1, three Boards of Participants were formed, each focusing on specific management issues. These Boards consisted of DA franchisees and were supposedly introduced in order to discuss more strategic issues with management¹. However, management¹ actually created these groups with a view to using them to build support among the group as a whole. As one manager said: *'I had already formulated my goals and incorporated them into the agenda for the meetings. I tried to get through ninety-five percent, and the rest I saved for the next meeting.'*

What franchisees wanted

There was a difference in opinion about the level of strategic participation between the small group of franchisees who were involved in strategic participation and the majority who were not. The franchisees who were closely involved were satisfied, while the majority of DA franchisees thought the strategic participation was badly organized and, therefore, participation was considered low. Some franchisees even talked about 'fake participation'. However, most accepted that the level of strategic participation was lower than they actually wanted because they felt they wanted enough freedom to run their business as they saw fit. However, when the requirements increased, strategic participation became more important, and franchisees became increasingly annoyed with the low level of strategic participation (see also section 5.7). The franchisees perceived strategic participation as poorly organized due to a lack of procedures. These procedures can be divided into three types:

- Procedures for selecting franchisees to be involved. The majority perceived the selection procedure for strategic participation as 'unfair'. Several franchisees who had served on one of the Boards of Participants said that they had been approached by Dynaretail to join one of the boards. According to management¹ and these members, many druggists were unwilling to do so. On the other hand, franchisees complained that the franchisees on the Boards were too heavily influenced by Dynaretail, because the management approached them to join the Board. Therefore, they did not expect these franchisees to represent their interests on the Boards.
- Procedures for replacing these franchisees. Franchisees who had been involved in strategic participation had served on the Boards for several years, which increased the other franchisees' perceptions of unfairness.
- Procedures relating to the rights of the Boards. The Boards of Participants had no formal rights, and the franchisees felt that management¹ did not listen to them. This was even felt by some franchisees who served on the boards. One of them said: *'It started off really well, and it was necessary. The druggists were able to take a look behind the scenes at Dynaretail, and expected that the management would listen to them. But then you really do have to listen to them, and the druggists thought they were not really being listened to.'*

Management¹ was aware that franchisees perceived strategic participation as poorly organized and, in 1997, the three Boards of Participants were combined in a new Policy Committee (in Dutch: beleidscommissie). However, several franchisees did not feel that this was an improvement because the procedures for the Policy Committee were still not set down in writing.

What actually happened

As already indicated, the franchisees' strategic participation was poorly organized due to a lack of procedures. Although the majority of franchisees wanted more highly organized strategic participation, this was not a major problem because they still felt they had a great deal of freedom in running their own businesses.

5.2.8 Strategic compatibility regarding the organization of franchisees' strategic participation during SCT2

What the franchisor wanted

Management2 thought that the governance of the Druggists' Association and Dynaretail/Dynadro had always been non-transparent. As previously mentioned, there had been different Boards and committees that influenced the DA system to a greater or lesser extent. As the CEO put it at the start of SCT2: 'Because of the variety of committees, certain topics are discussed by several committees, which makes the situation very unclear. One moment I'm discussing a topic with one committee, and the next moment I'm discussing it with another committee.' Apart from being unclear, the different committees resulted in a lack of decisiveness within the DA system, and the degree of strategic participation was perceived as low by the franchisees.

Management2 was aware of the difficulties with strategic participation. Therefore, it aimed for more efficient organization by establishing one management team, one Supervisory Board and one Board of Participants for the Druggists' Association and for Dynadro BV. The Supervisory Board had a supervisory task and the Board of Participants had an advisory task, and in some cases they had decision rights. The Board of Participants replaced the Policy Committee. The decision rights of this Board were established in the new Articles of Association of the Druggists' Association (dated 17 June 2003, see 5.1.3) and the new FSO. The fact that these rights were established in two separate documents can be explained by the fact that DA druggists were all members of the Druggists' Association (to which the Articles applied) and franchisees of the DA system that was administered by Dynadro (to which the FSO applied)³⁴. According to the Articles, the Board of Participants needed to approve decisions relating to the general management of the Druggists Association, cooperating or ending cooperation with other organizations, and introducing requirements for DA franchisees. According to the new FSO, the Board of Participants needed to give its approval whenever management2 wanted to introduce certain changes throughout the DA system.

What franchisees wanted

Most franchisees wanted strategic participation to be more efficiently organized in order to deal with the increasing requirements. They were aware that certain requirements would be introduced, and therefore considered it important that these should be approved by a Board of Participants representing their interests. However, franchisees differed in their expectations of whether this would really work. The majority thought that strategic participation would indeed improve because it would become more formalized, while others thought that increased formalization still would not work. According to them, a small group of franchisees in the form of a Board of Participants could not represent the interests of a very large and diverse group of franchisees. Additionally, there were franchisees who did not believe that management2 would comply with the procedures, and that it would continue to act as it had always been done in the DA system.

What actually happened

It was not possible to determine whether franchisees' strategic participation really became stronger during SCT2. However, during the development of the FSO, management2

³⁴ As presented in Fig. 5.1, the Druggists Association owned 100% of Dynadro's stock.

complied with the procedures for strategic participation that had already been established in the new Articles of Association.

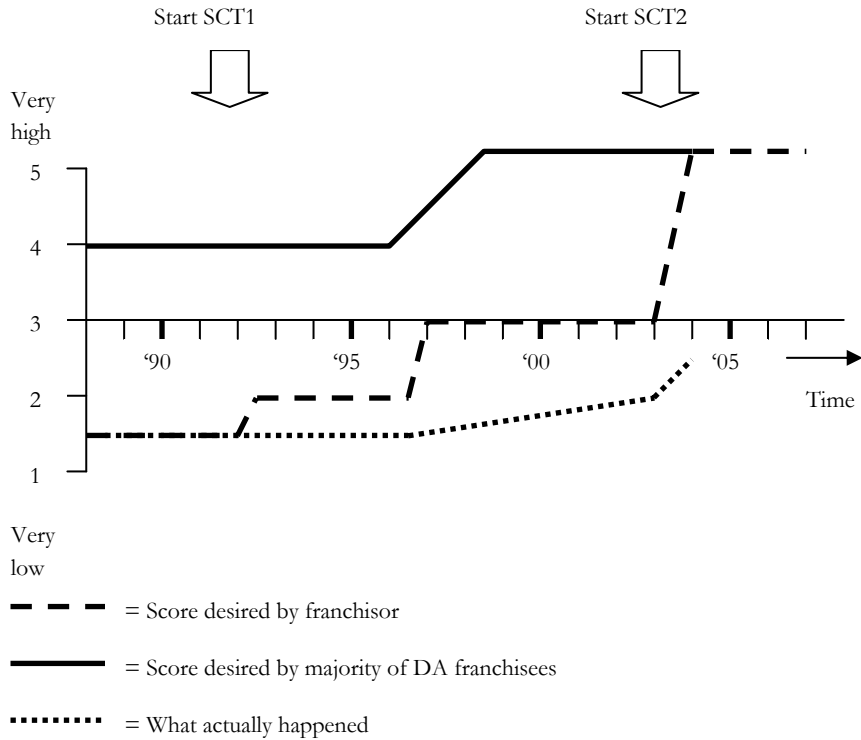


Fig. 5.6 Timeline for organization of franchisees' strategic participation

5.2.9 Strategic compatibility regarding type of growth objectives during SCT1

What the franchisor wanted

In the years before SCT1, the DA system had grown rapidly in terms of the number of stores, and growth had been largely quantitative. Although the DA system consisted of a large number of stores, the average floor area was relatively small. In 1992, the Dynaretail stores (DA, STIP, Eurodrogist and WPP) had an average floor area of 117 m². The floor area of the Dynaretail stores varied from 51 m² to 150 m². Management1 thought the average floor area was too low and wanted to increase it, along with turnover, so that the stores could implement the proposed requirements. Therefore, management1 aimed more at qualitative growth and wanted several franchisees to renovate and/or relocate in order to increase their floor area and turnover.

Related to the issue of quantitative versus qualitative growth were the criteria for the DA stores. Before the 1990s, there were virtually no selection criteria in place for DA franchisees. Although the Articles of the Druggists' Association stated that the Board could establish criteria for evaluating prospective DA franchisees, almost any independent

druggist could be admitted to the DA system³⁵. This resulted in a large and diverse group of DA franchisees. In order to realize more qualitative growth, management1 decided to implement selection criteria. One important criterion was the minimum floor area for stores.

Another aspect related to growth objectives was the management's aim to persuade DA franchisees with smaller stores to switch from the DA system to the STIP system, which was better suited to smaller stores. This would make the DA system more homogeneous in terms of store type, thereby facilitating the introduction of certain requirements and the realization of a certain level of hardness.

What franchisees wanted

Several franchisees did not want to relocate or renovate, which resulted in an incompatibility in growth objectives. However, because management1 did not strictly enforce the relocation or renovation requirements, this did not pose problems during SCT1.

With respect to the proposed switches to STIP, several franchisees with smaller stores did not want to do this. They did not want to switch from the well-known DA system to the unknown STIP system. Several of these franchisees saw the switch from the DA system to STIP as a 'downgrade', and thought they were not considered good enough to be a DA franchisee (see Chapter 6).

What actually happened

Management1 did not enforce the floor area increase or relocation, and this hindered its qualitative growth objectives. Moreover, because management1 did not really enforce a switch to STIP on smaller DA franchisees, several of them stayed with DA.

There were two factors that slightly stimulated DA's qualitative growth. First, other smaller DA franchisees did switch to STIP because they felt 'forced' to do so due to the increasing requirements at DA. Second, the general turnover³⁶ of the DA stores rose due to increased promotional activities.

5.2.10 Strategic compatibility regarding type of growth objectives during SCT2

What the franchisor wanted

Management2 wanted to integrate STIP, DA and DA D'Attance into a single DA system. The DA system would then increase from approximately 530 to approximately 730 DA stores if all the druggists remained, but the CEO expected several smaller DA franchisees to leave. For the new DA system, management2 also focused on qualitative growth rather than quantitative growth. According to the CEO of management2: *'I think that in 2007 we will have somewhere between 550 and 600 units with a larger average floor area than at present. This means that the total floor area will decrease, but its quality will increase. And productivity will increase too. The floor area for DA Basic stores is at least 100 square meters, and we are currently formulating other requirements. It's not only a question of floor area. We will try to find other locations for stores with a floor area of less than 100 square meters. That is how we will upgrade our stores. It will take us several years.'*

³⁵ The only reason why some druggists had not been accepted was that the Board did not expect their stores to be profitable.

³⁶ For management, turnover levels were relevant because the royalties were based on them, while for franchisees the balance between costs and turnover levels (profits) was relevant. The cost levels for franchisees increased during SCT1 (see section 5.3.1).

What the franchisees wanted

Several of the franchisees who were expected to object to the growth targets, i.e. franchisees with smaller stores, left the DA system shortly after the introduction of SCT2. In some cases, there were problems with growth objectives, but this was not on a large scale. Moreover, the change from STIP to DA Basic was an advantage for smaller DA franchisees for whom the STIP system actually had been more suitable. In the DA-basic format these stores could still operate under the DA name but with acceptable requirements.

One issue that was likely to cause problems with the integration of STIP into DA was the problem of 'duplication', i.e. two DA stores operating within a relatively small geographical area. However, at the time of the interviews for this study, this was not (yet) a problem because the STIP stores had not yet adopted the DA name, and franchisees expected few problems with that. Moreover, management did not expect many problems due to duplication.

What actually happened

The merging of the three systems resulted in one DA system with a large number of stores. In that sense, quantitative growth was achieved, although in a somewhat artificial way. However, management was actually aiming for higher qualitative growth in the future. It is too soon to determine whether this qualitative growth objective has been realized. However, relatively soon after the introduction of SCT2, several smaller franchisees left, thereby increasing the average floor area and average turnover of the DA stores.

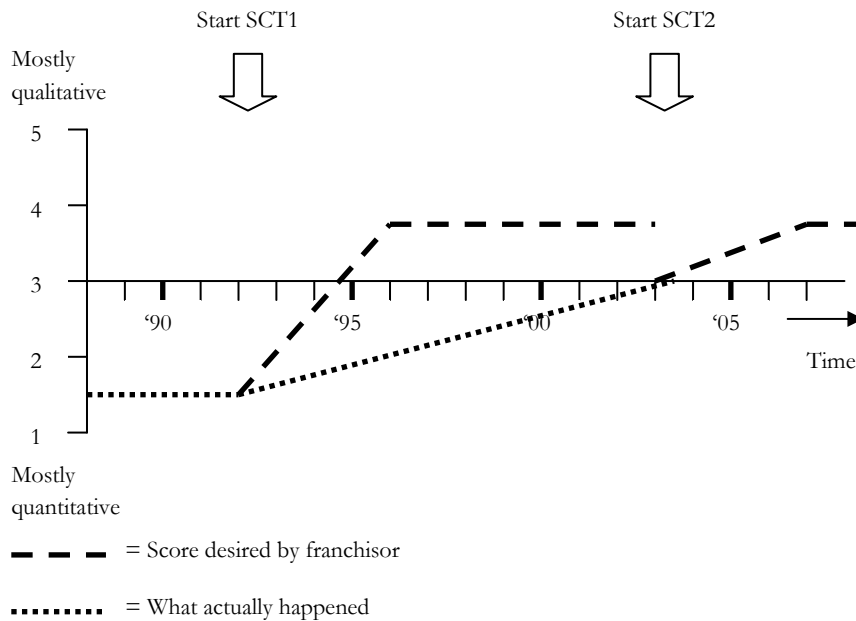


Fig. 5.7 Timeline for growth objectives in the DA system

5.3 Operational compatibility

5.3.1 Operational compatibility during SCT1: 'Toward business-format thinking'

The franchisees' perspective

With regard to the following factors, the franchisees perceived a low operational compatibility regarding the franchisor's capabilities (OC capa):

- Automation. Several franchisees were very dissatisfied with the automation process, despite the fact that they regarded automation as an important issue in the relationship. Dynaretail had tried to convince them to implement a particular automation system. Several franchisees had switched to this system but were not satisfied with it. Additionally, it had cost them a lot of money to switch to the new automation system.
- General support offered by the franchisor. Several franchisees claimed that people from Dynaretail had made mistakes during renovations or in certain calculations.
- Purchase prices. Several franchisees were under the impression that they could purchase more cheaply elsewhere (and did so).
- Logistics. There were few problems with respect to logistics; although several franchisees pointed out that the costs were high.

Although the franchisees were not completely satisfied with the franchisor's capabilities, they remained with DA because, in general, they did not expect things to be better in other organizations, and some of the problems were resolved relatively quickly.

With respect to operational compatibility regarding profitability OC profit, several franchisees thought the costs of participating in the DA system were very high. The most important costs during SCT1 were incurred through promotional activities for automatically supplied goods. Several DA franchisees considered their turnover to be relatively stable and, due to the level of competition, felt unable to attract extra customers and increase their turnover. Therefore, extra investment and costs were seen as undesirable. Every franchisee considered how far increased investment and costs would generate extra turnover and extra profits. One franchisee, who had switched from DA to UED just before the introduction of SCT2 said: *'The year is not over yet, but I think that our turnover has decreased. That's not surprising, because we no longer have the promotional campaigns every two weeks. We don't sell DA's brand products, which also means a decrease in turnover. On the other hand, costs and losses are lower. And I think that our net result at UED will be better than at DA. And that's what it's all about: the net result, not turnover.'*

Several franchisees gave DA a low rating for operational compatibility regarding trust/fair dealing (OC trust/fd). This was related to the perceived high cost of participating in the DA system. Several franchisees felt that the franchisor did not take their interests into account, and that their investments in the relationship were not in proportion to their benefits. They felt that the franchisor benefited more from the relationship than the franchisees, in other words: they had a perception of 'unfair dealing'. The most important cause for this was in the way the franchisor calculated the charges. Franchisees identified two problems with this:

- The use of ‘implicit charges’³⁷. Franchisees were under the impression that the franchisor aimed to receive extra royalties by charging higher prices for purchasing, automation and even for contracts with builders. Additionally, franchisees perceived these implicit charges to be very non-transparent. They did not know what the ‘actual’ costs and additional charges were, resulting in low OC trust/fd. One druggist who left DA said: ‘DA wanted to have traffic-builders in order to improve their price image. If that is not done by someone who is capable of doing it, you have the first problem. The second problem is that they bought in products for 50 cents, then added another 50 cents on the price for the druggists. They did that to keep the central organization sound. But then it became too expensive, and we couldn’t sell the products.’
- Calculations based on turnover. Because the charges were based on turnover levels, the franchisor benefited when franchisees generated high turnover. However, for franchisees the net result (turnover minus costs) was more important, so there was a conflict of interest. Several franchisees pointed out that the franchisor used the automatically-supplied goods to increase turnover, but overlooked the franchisees’ interests.

An additional issue mentioned by some druggists was the fact that the DA was a cooperative, and that the druggists who were members of DA should be sharing in the organization’s profits. The perception of these druggists with regard to fair dealing was even lower because they felt they were entitled to a share of the profits but had never received this.

The franchisor’s perspective

With respect to operational compatibility, the most important thing for the franchisor was that the franchisees were able to meet their financial requirements, i.e. the royalties and charges payable to the wholesaling organization (OC capa). Some franchisees showed only low profitability for the franchisor (OC profit) because they had a small floor area and/or made few purchases from the wholesaling organization. But this was not a problem during SCT1, provided these franchisees fulfilled their financial requirements.

OC trust/fd were not really issues for management¹ because it did not strictly enforce its requirements on the franchisees, which meant that franchisees could not be accused of ‘shirking’ their responsibilities. This applied to all types of requirement: business-format elements, purchasing, and automation. Because these elements were not really enforced, the franchisees could make their own decisions, and trust was only important in terms of the way in which franchisees presented the information used for calculating fees.

5.3.2 Operational compatibility during SCT2: ‘Integration and renegotiation’

The franchisees’ perspective

With respect to OC capa, automation was still an important issue, and was rated lowest by the franchisees. Additionally, franchisees perceived a low degree of OC capa for communication. This can be explained by the fact that SCT2 had just been introduced, and the franchisees wanted to know what the consequences of SCT2 would be for their stores, especially in terms of required investments (cost) and expected turnover. In other words,

³⁷ According to Caves and Murphy (1976), ‘implicit charges are an instrument by which franchisors can appropriate rents from franchisees. However, in the DA case this resulted in a perception of unfair dealing in the eyes of franchisees.

they wanted to know what their profitability (OC profit) would be after signing the FSO. Several franchisees did not dare to sign the FSO because they did not know what the cost of participation would be. According to management², it had no choice but to withhold this information from them because it did not want this information to become available to competitors. Additionally, management² tried to adjust the cost of promotional activities by calculating costs in a different way.

OC trust/fd was still low in the eyes of the DA franchisees. They did not trust the management because the cost of participation was not revealed until a very late stage. The franchisees were still afraid that the cost would exceed the benefits. One druggist, who left the DA system shortly after the introduction of SCT², said: *'The costs became too high for me: the cost of membership and promotional costs. It was just too expensive for me, and there were too few benefits. Margins decreased and the money went to head office, with its 150 employees.'*

The franchisor's perspective

With respect to operational compatibility with individual franchisees, the most important issue for the franchisor was still whether franchisees could meet their financial requirements (OC capa). This was a necessary condition for the franchisor. However, during SCT², tension arose between operational compatibility regarding profitability of franchisees (OC profit) and strategic compatibility regarding the degree of hardness (SC hard). Because management² wanted a higher level of hardness, it was sometimes forced to choose between strictly enforcing its requirements and letting go of profitable franchisees who did not wish to comply. The tension became particularly apparent when very profitable franchisees did not wish to comply.

It also became more important that the franchisor could trust franchisees not to 'shirk' their responsibilities, and that franchisees presented their financial situation in an honest way so that the franchisor could calculate the royalties.

5.4 Attractiveness of alternatives

5.4.1 Alternatives during SCT¹: 'Toward business-format thinking'

The franchisees' perspective

Becoming a franchisee of another drugstore system was an attractive alternative for several DA franchisees during SCT¹. In the nineties, several alternative drugstore systems developed. One of these was ETOS, which began its franchise operation in 1988. At the time, ETOS was a popular alternative for dissatisfied DA franchisees because ETOS was trying to attain a higher market position with its new Beauty Case format. The ETOS management was looking for franchisees in order to achieve this. Additionally, ETOS was known as a relatively hard system but, in order to attract new franchisees, its management accepted a lower degree of hardness (see section 8.1.2).

Besides ETOS, several drugstore wholesalers had begun to develop alternative franchise-like systems in the late 1980s and early 1990s, in order to create stronger links with their wholesale customers and to attract DA franchisees. These systems were ABC and DIO (Faco Diensten BV), Uw Eigen Drogist (Brocacef BV), De Vakdrogist (Vriesia BV), and De Drogist (Unipharma BV). The systems of Faco Diensten BV and Brocacef were the most popular among DA franchisees. They aimed to attract DA franchisees by emphasizing their softness and comparatively low cost level. Furthermore, several DA

franchisees already had had contacts with these firms through their wholesaling activities, which made it even easier for them to switch to these systems.

Another alternative for dissatisfied DA franchisees was the STIP system, which was managed by the same franchisor. Some DA franchisees switched to STIP because of the lower investment requirements, but they were not happy with it (see section 6.1.2). These franchisees left the DA system but did not end the relationship with the franchisor, while other franchisees wanted nothing more to do with the franchisor, and therefore switched to another franchisor.

The possibility of becoming a CID (completely independent druggist) was not very popular at the time. Some druggists joined the CREST group. This was a very loose form of cooperative, with circulating brochures, and joint purchasing for certain products. These druggists did not even operate under a common name (and I therefore classify them as CIDs). CREST began in 1981 and had always had around twelve members. In other words, this was a somewhat select group and entry was difficult for outsiders.

The possibility of starting a business in another industry – franchised or otherwise – was rarely seen as an alternative. Neither was becoming an employee of another organization, which was considered only as a ‘last resort’.

The DA franchisees had several considerations before them when evaluating the attractiveness of alternatives. The most important consideration was leaving the well-known DA name. Several DA franchisees were afraid that operating under an unknown name would result in fewer customers and lower turnover. However, the druggists who had already made the decision to switch from DA to another less well-known system said that they had fared better than they expected. In several cases, customers did not even notice that the druggist was no longer a DA store. And although turnover had fallen, costs had also fallen, ultimately resulting in higher profits.

The franchisor's perspective

From the franchisor's perspective, opening a company-owned unit was never seen as an attractive alternative. The only serious alternative for individual franchisees was to find a new franchisee for the store. However, there were several problems related to this. In several cases, the franchisee was the owner of the building, which meant, at that time, that the franchisee could simply continue in his own building with another drugstore system and wholesaler. In such cases, the franchisor would lose both the location and the wholesale customer. Moreover, it was often difficult for the franchisor to open a new DA store because the former DA franchisee would still be operating there, and the question was whether there would be enough market potential for two drugstores. In sum, when evaluating its alternatives, management had to deal with the tension between enforcing requirements and the risk of losing a location, a wholesale customer, and royalty payments.

5.4.2 Alternatives during SCT2: ‘Integration and renegotiation’

The franchisees' perspective

During SCT2, joining another drugstore franchise system was still the most attractive alternative. However, there had been a shift in the attractiveness of drugstore systems. In contrast to the SCT1 period, ETOS was no longer an attractive alternative, mainly because ETOS had also become a ‘harder’ franchise system. The DA franchisees saw ETOS as a hard franchise system in which they would have almost no freedom, and therefore considered it even worse than DA. Additionally, several DA franchisees expected that they

could not even join the ETOS system, even if they wished to. This perception was correct because, over time, ETOS had become very selective about which stores they wanted to attract as ETOS franchisees (see SCT6, Chapter 7). Moreover, at several locations of DA franchisees, an ETOS store was already operating.

The softer systems (Uw Eigen Drogist, DIO, ABC, De Drogist, de Vakdrogist) benefited a lot from the commotion at DA. These franchisors emphasized their softness and their high profit margins in specialist magazines and through personal visits to the DA stores. They attracted several DA franchisees in 2003 and 2004. Of the softer systems, Brocacef's UED system was the most attractive for DA franchisees. These DA franchisees expected that UED would become more powerful in time because it attracted several DA franchisees. Several franchisees who entered UED actually saw UED – and all the other soft drugstore systems – as not powerful enough, but they accepted this because they were so dissatisfied with DA. Moreover, in some cases the druggists simply copied other druggists; they thought that because another druggist had gone to UED, this was a good decision, and therefore decided to follow.

During SCT2, DA franchisees regarded becoming a CID as a difficult and time-consuming alternative. The CREST group was a small and select group of CIDs, which was considered an alternative by only a few DA franchisees. However, in February 2004 another alternative was launched for CIDs: the REZO group. This group did not operate under a common name; it had only brochures, joint purchasing for certain products, and its own brand that could serve as an alternative to DA brand products. REZO was started by a former manager of Dynadro who thought CIDs could still survive and even perform better than druggists in franchise-like cooperatives. During SCT2, several DA franchisees joined the REZO group.

One large DA franchisee considered another alternative as attractive, namely starting his own drugstore system. This franchisee already organized many things independently due to the large scale of his business. For example, he was an attractive negotiation partner for suppliers and made many independent agreements. Several druggists in the same geographical area knew about the plans to start the new system and contacted the druggist in order to join. However, this druggist eventually decided to stay with DA (see section 5.7.2).

During SCT2, the franchisees had several considerations before them when evaluating the attractiveness of alternatives. As during SCT1, the DA franchisees were afraid of leaving the well-known DA name, the strong DA brand products and the DA customer-loyalty program. They pointed out that they were afraid of the reactions of customers if they removed the DA name from their stores. One druggist who had just left the DA system said: *'Last Monday my husband was removing all the DA logos. I stood there and was worried. But we're located in a small village so the DA name is not so important. It makes a difference whether you're in a city or in a village. Here, the customers say "we're going to Harry's". They don't say "we're going to the DA".'*

DA franchisees were afraid that their turnover would fall if they left DA. However, they had heard from colleagues that, although their turnover would fall, costs would also fall, resulting in higher profits.

The franchisor's perspective

For management², there was still a tension between imposing requirements and the risk of losing a franchisee, wholesale customer, and a location. Management² argued that it no longer wished to make compromises, and it accepted losing franchisees in order to enhance uniformity. With respect to smaller stores, the franchisor kept to this policy. With respect

to more powerful and profitable franchisees – with larger stores or multiple stores – the tension was even greater because management² really wanted a higher degree of hardness, but in some cases this would mean losing a very profitable franchisee and/or several locations.

5.5 Switching costs

5.5.1 Switching costs during SCT1: ‘Toward business-format thinking’

The franchisees’ perspective

DA franchisees generally perceived switching costs as low during SCT1. First, investments in specific assets hardly played a role during SCT1. This was due to the large degree of freedom the franchisees had: they had never been forced to make specific investments in the DA system, for example, in terms of store interior, store exterior, or automation.

Second, there were few guarantees from the franchisor to persuade DA franchisees to stay. The only guarantee that played a role was the exclusive territory of the DA franchisees, which they would lose if they left the system. At the time, membership of the Druggists Association was for an indefinite period with a four-month period of notice. Several druggists had individual contracts with the wholesaler Dynadro, which resulted in other switching costs. With respect to the relationship with Dynadro, the Articles of the Druggists’ Association stated that a druggist could not terminate his membership of the Druggists’ Association if payments were still outstanding to Dynadro. In reality however, several druggists had been able to reach agreements with Dynadro in this regard, so this was not really a barrier to leaving the organization.

Third, with respect to percentage of total income, most of the franchisees earned 100% of their income from their membership of the Druggists’ Association, which raised the cost of switching. However, several franchisees who left DA expected their profitability to increase within the new system due to lower costs.

One aspect that can be added to the cost of switching based on the DA case is social/emotional bonds. Several DA franchisees mentioned ‘emotional switching costs’. Many DA franchisees had taken over the stores from their parents, who had often been DA druggists for a very long time. In some cases, the franchisees remembered this from their childhood. DA had always played a large role in their family life and they could hardly imagine a life without DA. A druggist who had been in the DA system for several decades said that the relationship with the DA felt like a marriage that you do not simply walk out on.

Another factor in switching costs that was not distinguished in the research model was the ease of entry into an alternative system. In the 1990s, ETOS aimed to attract DA franchisees by accepting a lower degree of hardness. This also meant that DA franchisees who switched from DA to ETOS did not have to make many specific investments, resulting in low entry barriers to the ETOS system. The same applied to the softer franchise-like systems: these did not require specific investments and their entry barriers were therefore low.

The franchisor’s perspective

In general, the cost of switching was also low for the franchisor. The franchisor had not made specific investments in individual franchisees. With respect to guarantees, these were highly dependent on the wholesale arrangements with individual franchisees, for example,

the franchisee purchasing a certain quantity of goods. The term of the relationship with DA franchisees was indefinite, but the Articles did stipulate situations in which the relationship could be terminated, for example in cases where a franchisee was not meeting his requirements. Here again, however, the franchisor had to choose between enforcing requirements and losing a wholesale customer, royalty payments, and a location.

5.5.2 Switching costs during SCT2: 'Integration and renegotiation'

The franchisees' perspective

When SCT2 was introduced, switching costs for most DA franchisees were still low. Specific investments were still low for a large group of DA franchisees because management¹ had never really enforced this requirement. Moreover, specific investments did not always result in high switching costs. One franchisee had already invested in the new DA 2005 format before SCT2. When he wanted to leave DA to switch to UED, neither the DA franchisor nor the UED franchisor made an issue of the fact that the franchisee did not alter the appearance of the DA 2005 store³⁸. This decreased this franchisee's exit barriers for DA and entry barriers for UED.

At the time of the introduction of SCT2, the franchisor was still providing few guarantees. Before signing the FSO, the short period of notice meant that it was still easy for franchisees to terminate the relationship with the franchisor. Some DA franchisees leased their locations via Dynadro, which constituted a further obstacle to leaving the organization. Franchisees who leased from Dynadro had to vacate the premises if they left DA. The franchisees who owned their premises could stay put if the relationship with Dynadro was terminated.

As pointed out in 5.5.1, several DA franchisees perceived emotional switching costs during SCT1. However, during SCT2, several of them argued that the emotional cost of switching had decreased over time, and they had started to look more objectively at their relationship with the franchisor.

An additional factor in the DA franchisees' reactions to the franchisor was the druggists' perception of the switching costs after signing the FSO ('future switching costs'). Signing the FSO would result in higher investment because certain investments became obligatory, and the FSO specified a minimum term for the contract with the franchisor. The duration of this term was a bone of contention and, under pressure from the druggists, the franchisor decided to decrease the duration of the FSO to two-and-a-half years.

The franchisor's perspective

During SCT2, the cost of switching was still generally low for the franchisor, due to absence of investment requirements and guarantees by the franchisees. In one case, a very large franchisee, who generated a significant percentage of Dynadro's income, wanted to terminate the relationship. In the view of management², the cost of switching was very high and it tried to retain this franchisee (see section 5.7.2).

³⁸ This was not a problem at the time of the interviews. It is possible that one of the franchisors would make a problem of this in a later stage.

5.6 Responses of the partners

5.6.1 Responses during SCT1: ‘Toward business-format thinking’

Responses of the franchisees

According to a manager under management1, the responses of the DA franchisees to SCT1 were as follows (see Fig. 5.8): covo = 15%, loy = 40%, negl = 25%, agvo = 10% and exit = 10%. The CEO of management1 gave a somewhat different estimation of franchisee responses: covo = 15%, loy = 60%, negl = 5%, agvo = 10% and exit = 10%. My own estimation for the responses after the introduction of SCT1 would be: covo = 15%, loy = 30%, amloy = 25%, negl = 10%, agvo = 10%, and exit = 10%. This estimate is based on the interviews with franchisees for SCT1.

The estimations of active responses are more or less similar, but there is a difference between the estimations for passive responses. A possible explanation is that it is more difficult to estimate passive responses because they are less visible to management than to the researcher. The difference between the estimates of the CEO and the manager can also be explained by the fact that the manager had closer contact with the franchisees, and therefore greater insight into their passive responses.

Moreover, the analysis in section 5.7 shows that the category of passive responses is more heterogeneous than initially assumed, which provides an additional explanation for the differences in the management’s estimations of passive responses. It is argued that the ‘ambiguous loyalty’ (amloy) response should be added. This response refers to situations in which franchisees waited to see what would happen before adopting further responses. I emphasize that these are the responses immediately after the introduction of SCT1, and that over time many franchisees switched to subsequent responses (see section 5.7).

Active			
Covo	Agvo	Exit	
15%	10%	10%	
15%	10%	10%	
<i>15%</i>	<i>10%</i>	<i>10%</i>	

Constructive		Destructive	
Loy	Amloy	Negl	
40%		25%	
60%	25%	5%	Normal: manager
<i>30%</i>		<i>10%</i>	Bold: CEO
			<i>Italic:</i> researcher
Passive			

Fig. 5.8 Estimations of responses of the DA franchisees for SCT1

Responses of the franchisor

During SCT1, management1 adopted covo toward franchisees who joined one of the Boards of Participants.

According to management1, it adopted covo toward all other DA franchisees in order to convince them to adopt the proposed changes. However, according to several franchisees, management1 adopted a passive response because it did not react to the franchisees' attempts to discuss the situation. Section 5.7 discusses the franchise partners' responses and their rationale in more detail.

5.6.2 Responses during SCT2: 'Integration and renegotiation'

Responses of the franchisees

The CEO of management2 gave the following estimation of the responses in a reaction to SCT2 (see Fig. 5.9): covo=10%, loy=35%, negl=35%, agvo=15% and exit=5%. The CEO said of these responses: *'The vast majority of the druggists are passive, but that could be consciously because they think they have other things to do. A passive person is difficult to assess. It makes a great deal of difference whether I, as the CEO, ask a druggist a question, or whether you, as a researcher, ask it. You might obtain different answers.'*

My own estimations for the responses to the introduction of SCT2 are as follows: covo=20%, loy=20%, amloy=20%, negl=15%, agvo=15% and exit=10%. These are based on the interviews with franchisees for SCT2. The amloy response for SCT2 is included, which again explains the differences between the estimations of the CEO s and the researcher (see section 5.7.2).

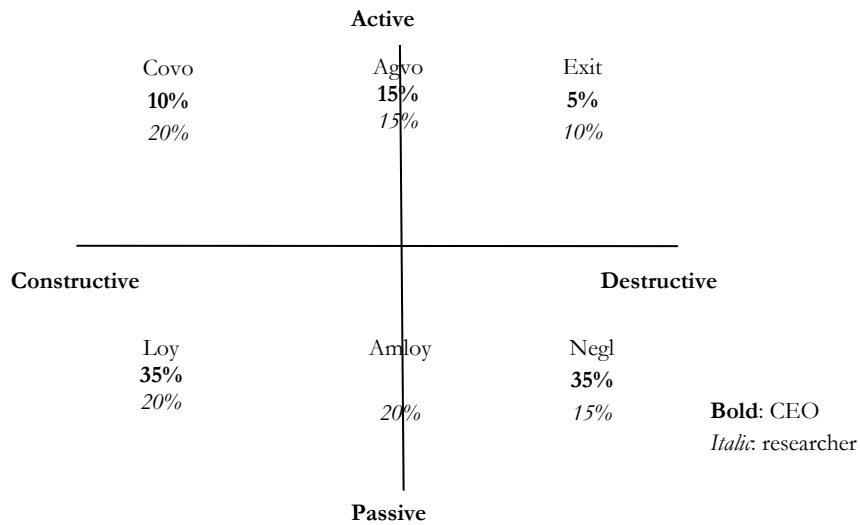


Fig. 5.9 Estimations of responses of the DA franchisees for SCT2

Responses of the franchisor

Management2 responded differently to individual franchisees. During the development and refinement of the FSO, management2 had held discussions with several committees of

franchisees, and negotiated the contract terms with these committees. That is a covo response.

During SCT2, management2 said it would no longer accept compromises, and the franchisees who did not want to sign the FSO would have to leave. Management2 argued that in such cases it was willing to adopt an exit response by itself. Section 5.7 discusses the responses of the franchisor and individual franchisees, and provides detailed insight into franchise partners' motives for the various responses.

5.7 Analysis of relationships between variables

Sections 5.2 to 5.6 have described the developments during SCT1 and SCT2 and the franchise partners' perceptions of the independent variables in general (leading to conclusions of type 1). The following section will take a closer look at the individual franchise relationships by analyzing relations between the independent variables and the responses (leading to conclusions of type 2). For SCT1 and SCT2, the development in franchisees' responses is presented in figures (Figs. 5.10 and 5.11), in which each number represents an individual franchisee. Each response type ('X-response' as example) will be discussed according to the following structure:

- Responses preceding the X-response (broken lines in Figs. 5.10 and 5.11).
- The X-response as initial response (bold numbers in Figs. 5.10 and 5.11). This will be the focal point of analysis in which the determining variables (see section 4.3.5) and the franchisees' perceptions of these variables are discussed in order to explain why they adopted the X-response.
- Subsequent responses to the X-response (unbroken lines in Figs. 5.10 and 5.11).

Additionally, the franchisor's responses and determining variables are discussed for each franchisee response type.

One limitation of Figs. 5.10 and 5.11 is that they do not indicate the time interval between the switches from one response to another. In fact, the intervals varied from a few weeks or months to several years. For a better understanding of the development of the responses, these intervals are discussed in the text.

For the meaning of the abbreviations, I refer to Appendix 11.

This section discusses the franchise relationships on a very detailed level. To readers who are interested on a more general level, I recommend to skip this section and to continue with section 5.8 in which the general conclusions for the DA system are discussed.

5.7.1 Analysis for SCT1: 'Toward business-format thinking'

Table 5.1 presents a summary of the data for SCT1. It presents the number of respondents (franchisees), the modus of the respondents' perceptions on the independent variables, and the modus of franchisor's responses for each response type. The thirteen respondents for SCT1 consist of: five covo franchisees, four loy franchisees, two amloy franchisees, one negl franchisee and one agvo franchisee. Table 5.1 shows that none of the respondents initially adopted exit. However, seven of the thirteen respondents for SCT1 eventually left the DA system. In the interviews, the respondents were asked in detail about the development of their franchise relationships over time and their reasons for eventually leaving. This made it possible to include the exit response in the analysis.

Res- ponse FRE	Strategic compatibility (SC)					Operational compatibility (OC)					Swico	Res- ponse FRO
	SC Pos	SC Hard	SC Innov	SC Org	SC Growth	OC Capa	OC Profit	OC Trust/ fd	Attalt			
Covo N=5	High (-)	Med (+)	Med (+)	Very high	NP ³⁹	Med	High	Med- high	Very low	Very low	Med	Covo
Loy N=4	High (-)	High (+)	Med (+)	Very high	NP	Med	Med	Med	High	Med	Med	Loy
Amloy N=2	Med/ very high (+)	Med (-)	Very high	Low (+)	NP	Very high	Med	Med	Very low/ low	Very low/ low	Med	Loy
Negl N=1	Med (+)	Med (-)	Low (+)	Low (+)	NP	Low	Med	Med	High	Low	Low	Negl
Agvo N=1	Low (+)	Low (+)	Med (-)	Low (+)	NP	Med	Very low	Low	Med	Low	Low	Negl
Exit N=0	-	-	-	-	-	-	-	-	-	-	-	-

Table 5.1 Summary of data for SCT⁴⁰

³⁹ 'NP' means that there were no problems with respect to the type of growth objective. 'p' means that there were problems.

⁴⁰ As section 4.3.5 pointed out, the + and - indicate whether the franchisees aimed for a higher (+) real score on the franchise system characteristics or a lower score (-). For example, med (+) on SC hard means that the franchisees perceived a medium degree of strategic compatibility on degree of hardness and actually wanted the degree of hardness to be higher.

Fig. 5.10 depicts the developments in the responses of individual franchisees to SCT1.

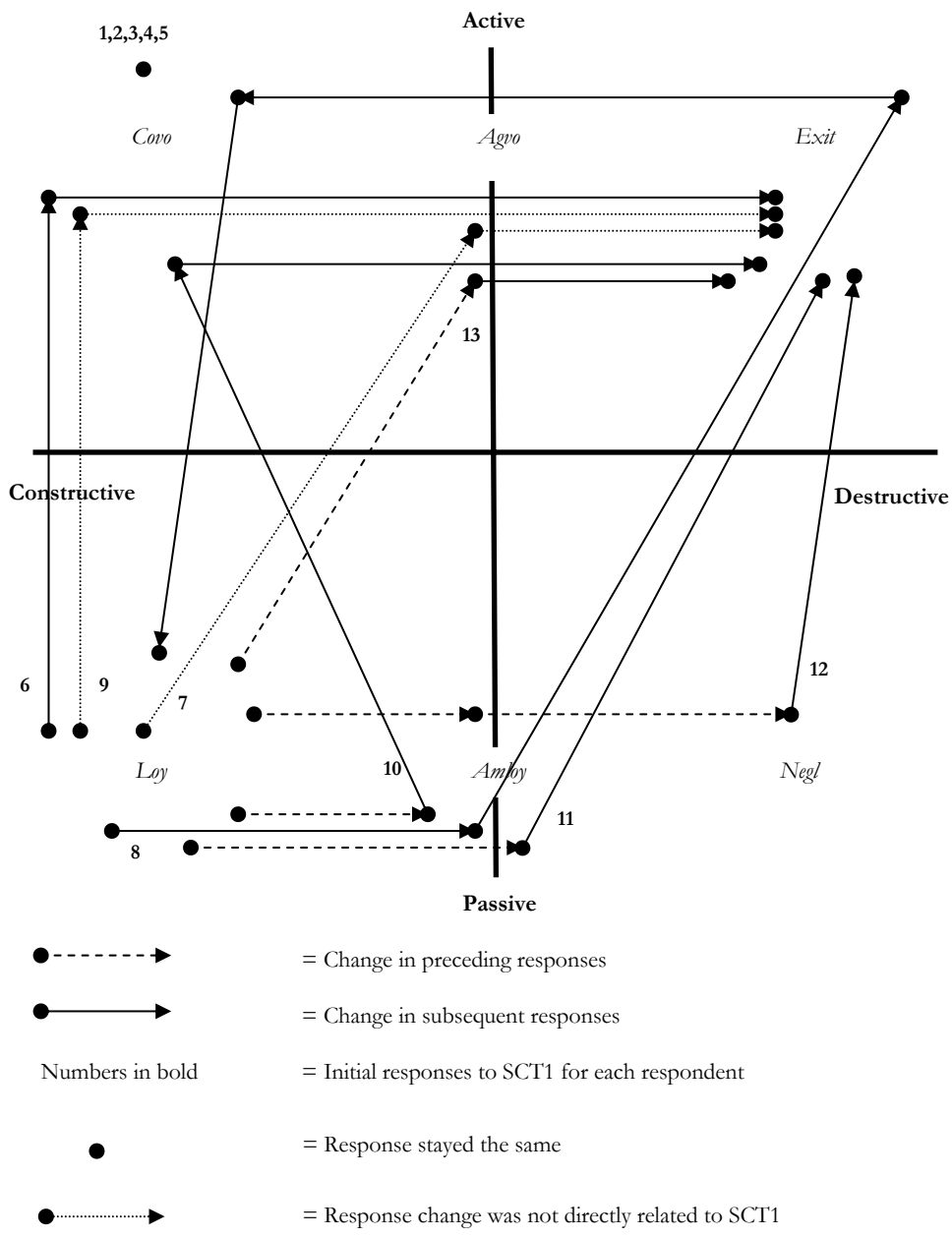


Fig. 5.10: Development of franchisees' responses for SCT1

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Responses preceding covo

Fig. 5.9 shows that franchisees 1 to 5 initially adopted covo (see numbers in bold). They joined one of the three Boards of Participants to discuss the proposed SCT1 requirements with management1. They were either asked by management1 to become more involved, or they had volunteered in response to a general request by management1. In many cases, they had already been active within the Druggists' Association before the start of management1 and, therefore, almost automatically adopted covo.

Covo as initial response

These franchisees' covo can be explained by their determining variables and their perceptions of these variables. In general, they agreed with the objectives of management1, and therefore expected a higher degree of compatibility in the future. They adopted covo to further discuss the plans with management1. Their determining variables were as follows:

- OC profit. They expected that a better-known brand name, with a certain positioning and rate of innovation, would attract more customers and increase their turnover and profitability. They therefore expected OC profit to increase once requirements were introduced.
- SC hard. They perceived a medium SC hard and wanted the level of hardness to increase because they were experiencing increased competition, which meant that they would need a well-known brand name and a certain identity in the near future in order to survive. A shared identity could be achieved only if more requirements were introduced for all DA franchisees. This was in agreement with the goals of management1.
- SC pos. These franchisees wanted DA's shared identity to take the form of a slightly lower positioning, which was in agreement with the goals of management1. The shared identity involved a slightly lower positioning because they expected it to attract more customers. For the DA system to have a lower positioning, these franchisees considered it important that all DA franchisees comply with certain requirements.
- SC innov. These franchisees wanted a slightly higher rate of innovation in order to attract more customers. In order to achieve this, they considered it important that all franchisees comply with certain requirements.
- OC trust/fd. This variable became more important after the introduction of the requirements because the (slightly) increased requirements would result in greater dependency on the franchisor. Since the circulation frequency of brochures and the quantities of automatically supplied goods increased soon after the introduction of SCT1⁴¹, OC trust/fd quickly became a more important variable. The covo franchisees' perception of OC trust/fd was high. It is interesting that only the covo franchisees perceived OC trust/fd as medium to high, while other respondents perceived this as lower. An explanation for this is the fact that the covo franchisees were involved in strategic participation and had close relationships with management1, and therefore knew more about management1's intentions.
- SC org. This variable also became more important due to the increased requirements. The covo franchisees agreed with the introduction of more

⁴¹ Before SCT1, there had already been some brochures with goods attached to them, but during SCT1 this was introduced on a larger scale.

requirements, but wanted to influence the *content* of these requirements and therefore started considering SC org as more important. They perceived SC org as very high, which is interesting because all the other respondents perceived it as low. An explanation for this is that the covo franchisees themselves were involved in the process of strategic participation through the Boards of Participants.

SC growth was not a determining factor for these franchisees because management did not force them to renovate or relocate, and there were no problems with exclusive territories. OC capa was not a determining variable for the covo franchisees for three reasons. First, there were few requirements for these factors (such as purchasing and automation), and franchisees still had considerable freedom to obtain these in another way. Second, they perceived that most of the problems concerning the franchisor's capabilities were often solved relatively quickly. Third, they did not expect the capabilities of another franchisor to be any better, or better than if they carried out the activities themselves.

The covo franchisees perceived the attractiveness of alternatives (attalt) as very low. This is interesting because it differs greatly from the negl and agvo franchisees, who rated the attractiveness of alternatives as medium or high. There are two explanations for this. First, the covo franchisees did not really consider possible alternatives because they perceived the current relationship as very attractive and had therefore had never seriously considered the alternatives. Second, the covo franchisees considered other types of alternatives as relevant compared to the negl and agvo franchisees, who considered a well-known brand name to be less important. Because the covo franchisees favored a well-known brand name and a certain market identity, they had a limited range of alternatives to choose from.

The covo franchisees mostly perceived switching costs as low. However, switching costs were not a determining factor for them because they were satisfied with the relationship and did not feel the need to switch to an alternative.

Management1 adopted covo toward these franchisees because it believed these franchisees could help to build support for the changes among the larger group of franchisees ('Creating support', Table 5.2).

Responses subsequent to covo

Franchisees 1 to 5 did not change their responses over time and maintained covo. They had such close relationships with management1 that they automatically raised issues with the management in a proactive way.

Responses preceding loy

Franchisees 6 to 9 initially adopted loy upon the introduction of SCT1 (see bold numbers in Fig. 5.9), and their preceding responses had always been loy responses because they had always been satisfied with DA.

Loy as initial response

For these franchisees, the determining variables were the same as for the franchisees who initially adopted covo:

- OC profit. These franchisees also expected that a better-known brand with a certain positioning and faster innovation would attract more customers and increase their profitability (OC profit). However, they perceived certain thresholds: more requirements would require more investments and higher costs, which in turn would require higher turnover in order to increase or maintain profitability.

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- SC hard. They considered a well-known brand name as important and agreed with the introduction of increased requirements on positioning and the rate of innovation.
- SC pos. They expected the lower positioning to attract more customers, which would increase their profitability. They expected a higher SC pos in the future and did not feel the need to adopt an active response.
- SC innov. They perceived a medium SC innov because they wanted the rate of innovation to be higher. Because management¹ also wanted a higher rate of innovation, these franchisees expected a higher SC innov in the future and did not feel the need to adopt an active response.
- OC trust/fd. For the loy franchisees, OC trust/fd also became more important due to the increased requirements. Because there were relatively few requirements in the early phases of SCT1, franchisees accepted a medium OC trust/fd. However, as we will see, when requirements increased further, a medium OC trust/fd became a problem for certain franchisees, who then switched to another response.
- SC org. The same applies to SC org, which had also become more important due to the increased requirements. In the early phases of SCT1, the franchisees were aware that they still had a great deal of freedom in running their businesses, and they therefore considered strategic participation as less important. However, when the requirements increased further, in their view SC org became more important.

OC capa and SC growth were not determining variables because the franchisees still had a great deal of freedom in doing this independently, and incompatibility with the franchisor was therefore less important.

Management, in turn, adopted loy toward the loy franchisees because it expected them to adopt the proposed requirements (and therefore a high SC hard).

Responses subsequent to loy

Franchisees 6 to 9 subsequently switched to other responses. For franchisees 7 and 9, this switch was not directly related to the development in SCT1 but was due to other conflicts with the franchisor, which eventually led them to leave DA.

Franchisees 6 and 8 switched to other responses because of the changes during SCT1. At the start of SCT1 they had accepted the requirements, but eventually reached a threshold due to the increased requirements in the later years of SCT1. Franchisee 6 felt forced to adopt covo because he perceived a decreasing OC profit, which was related to the increasing cost level. This, in turn, was due to the way in which royalties were calculated⁴². Management did not react to franchisee 6's attempts to discuss the problems. In reaction to the franchisor's negl, franchisee 6 adopted exit. Management adopted negl because it expected that this franchisee would not comply with the increasing requirements (SC hard). It is interesting that management allowed this franchisee to leave, given that he had several locations and paid a lot of royalties to DA.

Franchisee 8's loy response became increasingly 'ambiguous' in the years after the introduction of SCT1: he increasingly doubted the value of DA in terms of his profitability

⁴² This franchisee had both DA and DA D'Attance stores, and his turnover was relatively high because he sold considerably more perfume compared to other DA stores. Royalties were calculated on the franchisee's turnover (including luxury perfumes). However, he thought that DA's and DA D'Attance's promotional activities did not increase turnover for perfumes. Therefore he left DA and DA D'Attance.

(OC profit) and eventually left DA. This departure was triggered by the introduction of SCT2, in which he was supposed to sign the FSO, and is therefore further discussed in SCT2 (franchisee 10 for SCT2).

When adopting a response toward franchisees who did not want to adopt the proposed requirements, management1 had to deal with certain tensions. It wanted a certain degree of hardness and therefore SC hard was very important. However, some franchisees did not want an increasing degree of hardness and did not want to comply with the requirements. This would result in a low SC hard from the franchisor's perspective. However, these franchisees were a source of income for the franchisor in terms of royalty payments, and also because they were (or at least supposed to be) wholesale customers of the franchisor. In other words, individual franchise relationships had a certain profitability for the franchisor (OC profit). Especially in cases where the franchisee made a significant contribution to the franchisor's total income, the cost of switching (swico) was high for the franchisor. Additionally, the loss of a franchisee also meant the loss of a store location, and the franchisor took this into account when adopting a response.

Responses preceding amloy

Franchisees 10 and 11 had always adopted loy because they had always been satisfied with DA. However, when SCT1 was introduced they switched to an 'ambiguous loyalty (amloy)' response, which means that they were in doubt as to how to react to the introduction of SCT1 and were waiting to see what would really happen before adopting another response. The amloy response is actually a separate type of passive response: it is more destructive than loy but less destructive than negl. This finding led to the inclusion of amloy as a separate response type in the model. Therefore, it is included as a new response type in Figs. 5.10 and 5.11 and is also considered in Tables 5.1 to 5.4.

Amloy as initial response

Franchisees 10 and 11 were satisfied with the relationship as it was when SCT1 was introduced, but they waited to see how their perceptions of the determining variables would develop in the future. Their determining variables were the following:

- OC profit/cost. This is actually a variation on OC profit. These franchisees emphasized their cost level as an element of profitability and that is why it is referred to here as OC profit/cost. They emphasized their cost level because they considered their turnover to be stable. This had to do with their perception of the level of competition, which is an important background variable (see section 5.8.3). They did not believe that they could improve their turnover and profitability through extra investment and costs. For these franchisees, the increasing degree of hardness and the cost level were related, and increasing the degree of hardness was undesirable because it would increase the cost level without resulting in higher turnover.
- SC hard. Franchisees 10 and 11 expected the increasing degree of hardness to result in higher costs and therefore reduced profitability (OC profit). Therefore, they did not want the degree of hardness to increase in the future, which was the opposite of what management1 wanted.
- SC pos. These franchisees also objected to a lower positioning because it did not fit with their local circumstances. Additionally, the promotional activities to support this lower positioning were obligatory, which resulted in high costs for them.

- SC innov. The same applied to the rate of innovation. Franchisees 10 and 11 considered a high rate of innovation as unnecessary for their stores. However, the rate of innovation would increase as more requirements were introduced. They considered this as acceptable (within certain boundaries) for new products because it required relatively low investment. However, a higher rate of innovation required more investment, and they considered this unacceptable. Since this higher rate of innovation was not enforced by management¹, this did not pose problems at the time.
- OC trust/fd. OC trust/fd had become more of a determining factor in the eyes of these franchisees due to the slight increase in requirements. However, because OC trust/fd still was rated as medium at the time, this did not pose problems.
- SC org. This had also become more of a determining factor due to the increased requirements because the franchisees wanted to influence the content of the requirements. Franchisees 10 and 11 perceived this as low, but did not really consider this a problem because their perception was that they were still allowed considerable freedom in running their businesses.

OC capa and SC growth were not determining factors because the franchisees still perceived freedom within them, and there were no problems with exclusive territories (as part of SC growth).

The most plausible explanation for these franchisees' amloy, as opposed to an active response, to the introduction of SCT1 is that the consequences of SCT1 were not yet clear to them when SCT1 was introduced, and they could still deal with the consequences of the SCT in their own stores. Moreover, they perceived the attractiveness of alternatives as low, which might have influenced their response. Additionally, the franchisees' perception of medium switching costs might have been a reason for remaining within DA.

Management¹ in turn adopted loy toward the amloy franchisees because it expected them to adopt the requirements. It was not apparent to the management that the loyalty of these franchisees was ambiguous. Their dissatisfaction did not become apparent to management until these franchisees began to adopt an active response.

Responses subsequent to amloy

Franchisees 10 and 11 switched to an active response at a later point in time. They were prompted to switch from loy to a subsequent active response because they reached a threshold in terms of their determining variables. When the threshold was reached, the amloy franchisees were prompted to change to an active response toward the franchisor. Franchisees 10 and 11 adopted an active response at different times because their thresholds differed.

By adopting covo, franchisee 10 first tried to convince the franchisor to reduce cost levels, while franchisee 11 immediately adopted exit. However, management¹ mostly remained passive and allowed both franchisees to leave the DA system. Management did not respond actively because it considered these franchisees' stores to be too small and expected a low SC hard in the future. Moreover, because OC profit was not very high, the franchisor could easily allow these franchisees to leave.

Responses preceding negl

Franchisee 12 initially adopted negl to the introduction of SCT1. He had taken over the store from his parents, who had always been very satisfied with DA. After he took over the store in the 1980s, he noticed that the participation costs were gradually increasing due to

brochures and automatically supplied goods, and he gradually switched from amloy to negl as an initial reaction to SCT1.

Negl as initial response

For franchisee 12, the determining variables were the same as for the amloy franchisees (10 and 11), and for the same reasons:

- OC profit/cost.
- SC hard.
- SC pos.
- SC innov.
- OC trust/fd.
- SC org.

OC capa was not a determining variable because management did not enforce the use of the franchisor's services. SC growth was not a determining factor because growth objectives were not enforced by the management.

The difference between the negl and amloy franchisees probably related to their threshold with respect to these variables. The threshold was lower for the negl franchisee than for the amloy franchisees, which explains why he switched more quickly to a more destructive response.

In the years after the introduction of SCT1, franchisee 12 still gave a medium – as opposed to low – score for his determining variables, despite the fact that the management had very different objectives. During SCT1, he simply did not implement the proposed changes in his store, and management1 did not enforce the requirements, so the franchisee still perceived a great deal of freedom. In other words, due to the lack of strict enforcement by management1, this franchisee still experienced these scores for his determining variables as medium and therefore did not feel the need to adopt an active response.

It is interesting that, although this franchisee rated the attractiveness of alternatives as high, and switching costs as low, he still did not adopt exit at the time. An explanation for this is that strategic and operational compatibility were still above his thresholds (due to the lack of enforcement by management1), which is why he did not regard exit as necessary.

Responses subsequent to negl

Eventually, one 'trigger' caused him to switch immediately to exit. The trigger was a conflict that resulted in a very low OC trust/fd. His satisfaction with the relationship had slowly decreased over time, and this conflict was the trigger to leave immediately. This sudden exit was possible because the franchisee perceived the attractiveness of alternatives as high and the cost of switching as low. It is interesting to note that the negl response of the franchisee and the low enforcement by management1 had kept his switching costs low because he had not made any specific investments. However, according to this franchisee, even if the switching costs had been high, he would still have left the DA system because he had become very dissatisfied.

Management1 had mostly adopted negl toward this franchisee. As pointed out, it had not tried very hard to enforce the requirements. After the franchisee had notified the franchisor that he wanted to leave, management1 even tried to speed up his departure by proposing a shorter term of notice. Management1 considered him a 'difficult' franchisee who would not adopt the proposed requirements, which would result in a low SC hard in the eyes of the franchisor.

Responses preceding agvo

Franchisee 13 adopted agvo immediately after the introduction of SCT1. Before SCT1, he had always been satisfied with DA and had adopted loy toward the franchisor. However, he felt 'shocked' after the introduction of SCT1. The way in which management1 introduced SCT1 gave him the impression that there was no room for negotiation, and that his future perceptions of his determining variables would become more unfavorable. With agvo, he tried to convince the franchisor not to implement the proposed changes.

Agvo as initial response

The determining variables were the same for the agvo franchisee as for the amloy and negl franchisees, for the same reasons. However, the agvo franchisee expected that management would introduce the requirements quickly and that his threshold of his determining variables would be reached very soon. He therefore adopted an active response almost immediately. The most important issues were the increase in costs (resulting in low OC profit/cost) and the increasing degree of hardness (resulting in low SC hard). In this franchisee's view the degree of hardness was related to the cost level because more requirements required higher investments and therefore higher cost levels. Even more importantly, this franchisee regarded himself as an independent business owner. Therefore, SC hard was placed first in Table 5.2. Moreover, he did not want to sell the non-drugstore-related goods because they did not fit into the trade of the druggist.

It is interesting that his perceptions of OC trust/fd and SC org had always been low, but this had not mattered to him until the degree of hardness actually increased. According to the franchisee, this happened very soon after the introduction of SCT1. In other words, SC org and OC trust/fd became determining variables for this franchisee when the actual degree of hardness had increased in his perception.

Responses subsequent to agvo

Once the agvo franchisee found out that his agvo did not affect the plans of management1, and that his perceptions of the determining variables had become low within a short period of time, the franchisee quickly adopted exit.

Because he had become so dissatisfied with the DA system, franchisee 13 accepted a 'mediocre' alternative. According to him, management1 adopted negl by letting him go very easily because he was seen as an 'annoying' franchisee. In this situation, too, management had to deal with the tension between enforcing the requirements and the profitability of the relationships. In this case, SC hard was more important to management because it simply allowed this franchisee to leave.

Exit as a subsequent response

As already mentioned, none of the respondents adopted an exit response as an initial response to SCT1, but seven of the thirteen respondents adopted it as a subsequent response. The departure of two of the franchisees had nothing to do with SCT1 but was due to other conflicts with the franchisor (numbers 7 and 9 in Fig. 5.10).

As Fig. 5.9 shows, franchisees 6 to 13 adopted exit as a subsequent response. Franchisees 7, 9, 10, 12 and 13 left because they experienced an 'unbearable situation' and felt 'forced' to leave because they felt this was inevitable for the successful continuation of their business. By contrast, franchisees 6, 8 and 11 adopted exit mainly because they felt they had a better and less costly alternative. They did not really feel forced to leave, but were 'pulled' toward another alternative. The eventual exit of franchisee 8 is discussed under SCT2 because he adopted exit immediately after the introduction of SCT2.

For franchisees 7, 9, 10, 12 and 13, the situation had become financially unbearable: the low OC profit/cost and SC hard were the most important determining variables, and all other variables were related to these. The increasing requirements concerning positioning and rate of innovation had caused costs to increase, and SC pos and SC innov had become determining variables. The extra requirements had increased the cost level. Additionally, due to the increasing degree of hardness, the low OC trust/fd and the low SC org had become determining factors. For franchisees 7 and 9, the 'unbearable' situation also resulted from problems of trust between the partners: due to a conflict, they felt that the trust relationship had been damaged beyond repair. Franchisees 7, 9, 10, 12 and 13 mostly perceived a low to medium attractiveness for alternatives, but they accepted a 'lesser' alternative because they felt forced to leave DA. In other words, the attractiveness of alternatives was not a determining variable for these franchisees. The same applied to the cost of switching: because the franchisees felt forced to leave, the high level of switching costs was relatively unimportant.

Franchisees 6 and 11 did not really feel forced to exit DA, they simply perceived a better opportunity elsewhere. For them, OC profit and the attractiveness of alternatives were the determining variables. They expected to realize more profit in another way. They perceived switching costs as low, but switching costs were considered less important because they perceived a very attractive alternative. However, as will be shown for SCT2, they accepted switching costs within certain parameters.

The responses of the franchisor toward franchisees 7, 9, 10, 12 and 13 were mostly negl because the franchisor regarded these franchisees as too small to keep pace with the desired degree of hardness (resulting in low SC hard), too small to be very profitable (low OC profit), and regarded them as franchisees who might even have difficulty in meeting their future financial requirements (low OC capa). Management adopted negl toward franchisees 6 and 11 because it thought that they did not agree with the increasing degree of hardness anyway, which would result in a low SC hard. In these situations, the franchisor perceived SC hard as more important than the profitability of the franchisee.

Summary of determining variables

Table 5.2 presents the determining variables for each response, in order of importance.

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Determining variables for franchisees' responses in order of importance					
Covo	Loy	Amloy	Negl	Agvo	Exit
Franchisees 1 to 5 ('voluntary'): OC profit SC hard SC pos SC innov OC trust/fd SC org SC growth	OC profit SC hard SC pos SC innov OC trust/fd SC org	OC profit/cost SC hard SC pos SC innov OC trust/fd SC org	OC profit/cost SC hard SC pos SC innov OC trust/fd SC org	SC hard OC profit/cost SC pos SC innov OC trust/fd SC org	Franchisees 7,9,10,12,13 ('forced'): OC profit/cost SC hard SC pos SC innov OC trust/fd SC org
Franchisee 6 ('forced'): OC profit					Franchisees 6,11 ('voluntary'): OC profit Attalt
Determining variables for franchisor's responses (to franchisees' responses) in order of importance					
Franchisor's response to 1 to 5 = covo (creating support)	Franchisor's response to loy = loy OC capa SC hard OC profit	Franchisor's response to amloy = loy OC capa SC hard OC profit	Franchisor's response to negl = negl OC capa SC hard OC profit	Franchisor's response to Agvo = negl OC capa SC hard OC profit	Franchisor's response to 7, 9, 10, 12, 13 = negl OC capa SC hard OC profit
Franchisor's response to 6: OC capa SC hard OC profit					Franchisor's response to 6 and 11 = negl OC capa SC hard OC profit

Table 5.2 Summary of determining variables for each response type in order of importance for SCT1

5.7.2 Analysis for SCT2: 'Integration and renegotiation'

Table 5.3 presents a summary of the data for SCT2. For each response type, it presents the number of respondents (franchisees), the modus of these franchisees' perceptions of the independent variables, and the modus of franchisor's responses. The sample consisted of twelve franchisees: six covo franchisees, one amloy franchisee, one negl franchisee, one agvo franchisee and three exit franchisees.

	Strategic compatibility (SC)						Operational compatibility (OC)					Attalt.	Swico	Resp. FRO
	SC Pos	SC Hard	SC Innov	SC Org	SC Growth	OC Capa	OC Profit	OC Trust /fd	OC Capa	OC Profit	OC Trust /fd			
Resp. FRE N=6	Very high	High +	High (+)	Very high	NP	Med	High	Med	High	Very high	Very low	Very low	Very low/low	Covo
Loy N=0	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Amloy N=1	Very high	Med +	Med +	Med +	NP	Med	High	Med	High	Med	Low	Low	Med	Covo
Negl N=1	Low +	Low -	Low -	Low +	NP	Low	Low	Very low	Low	Low	Low	Low	High	Negl
Agvo N=1	Very high	Low -	Med	Low +	NP	Med	Low	Med	Low	Med	Very low	Very low	High	Negl
Exit ⁴³ N= 3	Low +	Low -	Med +/-	Low +	NP	Med	Very low/med	Low/med	Very low/low	Med	Low	Low	High	Covo

Table 5.3: Summary of data for SCT2

⁴³ This row in the table is misleading because the three exit franchisees were in very different situations. The situation is explained in the text, while Table 5.3 presents the scores for the situation of the majority of franchisees.

Fig. 5.11 shows the developments in the franchisees' responses to SCT2.

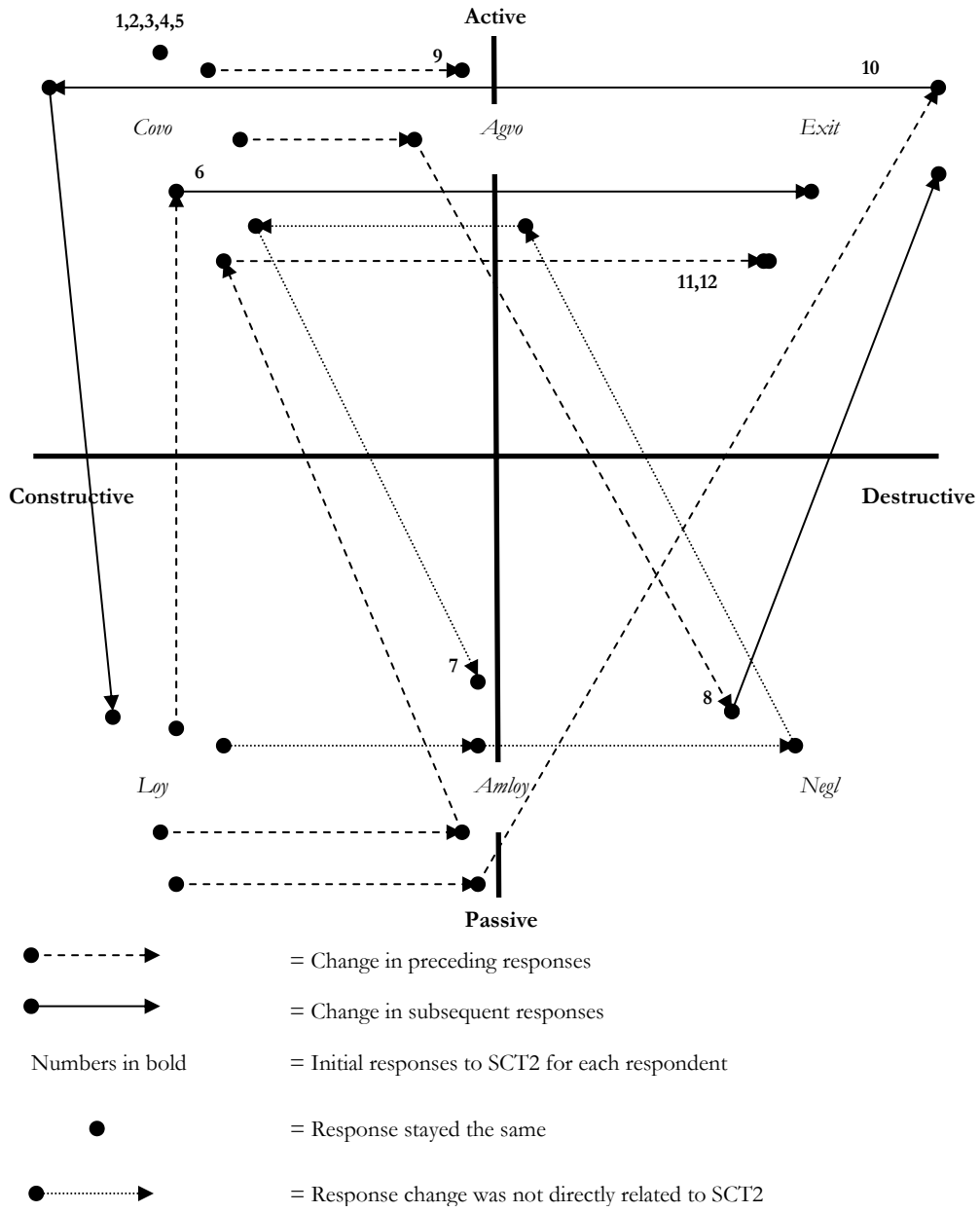


Fig. 5.11: Development of franchisees' responses to SCT2

Responses preceding covo

Franchisees 1 to 6 adopted covo as their initial response to the introduction of SCT2. Franchisees 1 to 5 almost automatically adopted covo because they had been involved in one of the Boards or committees that discussed certain issues with the management. Some of them had already been involved since the introduction of SCT1. Franchisee 6 had always adopted loy as preceding response but, when SCT2 was introduced, he felt forced to switch to covo.

Covo as initial response

Franchisees 1 to 5 and franchisee 6 differed in their motives for adopting covo. They differed mainly in their perceptions of their determining variables.

Franchisees 1 to 5 agreed with the objectives of management2, namely to continue to develop DA into a well-known brand name with a certain shared identity. Their covo involved discussing the exact plans with management2 and attempting to come to an agreement. Their determining variables were the following:

- OC profit. These franchisees expected that a better-known brand name with a certain positioning and rate of innovation would improve their profitability. They expected the changes of SCT2 to result in a very high OC profit.
- SC hard. They agreed with the introduction of the FSO because they thought DA needed to become harder in order to create a shared identity.
- SC pos. After signing the FSO, there would be many requirements with respect to positioning, and franchisees would have less freedom left to establish their own position. Therefore, SC pos became an even more important variable than for SCT1. The covo franchisees agreed with management's objectives for positioning and therefore perceived SC pos as very high.
- SC innov. This was the same as for positioning: once the FSO was signed, there would be many requirements with respect to adopting certain innovations. During SCT2, requirements applied to both the lower level (new products) and the higher level (other business-format adaptations and adapting the business format as a whole). Therefore, SC innov had become more of a determining factor than during SCT1. Franchisees 1 to 5 had the same goals as management2, i.e. a higher rate of innovation.
- OC trust/fd. Because the FSO contained many requirements, and franchisees would become more dependent on the franchisor, OC trust/fd became more of a determining factor for these franchisees. Franchisees 1 to 5 perceived OC trust/fd as very high, mainly because they were closely involved in strategic participation and understood the management's intentions and plans for SCT2.
- SC org. This had also become more important due to the increased requirements. Because several requirements were established in the FSO, these franchisees considered it important that they could influence the requirements through strategic participation. They perceived SC org as very high because they themselves were involved in strategic participation. As pointed out, other franchisees had mostly considered SC org as low in the past, but expected it to increase with the new corporate governance structure.
- OC capa. The FSO contained several requirements with respect to services that had to be taken from or via the franchisor, such as automation and purchasing. Therefore, OC capa became more important during SCT2 because franchisees became more dependent on the franchisor's capabilities with respect to these

services. However, this was considered less of a determining factor than the other variables because franchisees expected that problems with the franchisor's capabilities could be solved relatively quickly, and that these services would be no better if they were provided by another party or if the franchisee arranged them independently.

With respect to alternatives, franchisees 1 to 5 saw very few attractive alternatives to the DA system. Some of them argued that they did not care about alternatives because they were satisfied with DA and therefore did not feel the need to consider alternatives. Moreover, the covo franchisees perceived switching costs as 'very low' to 'low', which can also be explained by the fact that they had not really thought this through because they were satisfied with the relationship. Additionally, they pointed out that a high level of switching costs would not even influence their decision to adopt a certain response: if they should ever decide to leave DA in order to move to an attractive alternative, the costs of switching would not be very important.

Management2 in turn adopted covo toward these franchisees. It had involved these franchisees because it wanted to build support among the large group of franchisees for adopting the proposed changes of SCT2 ('Creating support' in Table 5.4).

As pointed out, franchisee 6 had other motives for adopting covo: he felt 'forced' to adopt covo. His determining variables were as follows:

- OC profit/cost. For this franchisee, the cost of participating was the most important factor because he considered his turnover to be stable. He thought that the costs of investing in a well-known brand name would not result in higher profits, and might even result in lower profitability. He expected that, after signing the FSO, his costs would rise so much that OC profit/cost would fall below his threshold.
- SC hard. According to this franchisee, the cost level and degree of hardness were related. To keep costs stable, the franchisee did not want the increasing degree of hardness. Given his competitive situation, he did not think that an increasing degree of hardness was necessary for his store (see background variables, section 5.8.3).
- SC pos. As pointed out, positioning became largely obligatory and therefore more of a determining factor. According to this franchisee, a lower positioning was not needed for his store. In the past, his experience had been that the brochures and related goods increased his costs, and he expected this to become even worse after signing the FSO.
- SC innov. After signing the FSO, the franchisee would be obliged to adopt certain innovations, despite the fact that he thought a higher rate of innovation was unnecessary for his store. On both the lower level (new products) and the higher level (other alterations and general business format), he considered this would require investment, which was not desirable because his turnover was stable.
- OC trust/fd. This also became more important due to increasing requirements, and he perceived this as low.
- SC org. This was considered important due to the increased requirements, but was perceived as low.

Franchisee 6 adopted covo because he wanted to know how the changes of SCT2 would influence his costs. However, when management ignored this response, the franchisee began to look for alternatives and switched to a softer drugstore system. He perceived his

switching costs as medium, and accepted this because he had found an attractive alternative.

During SCT2, management again had to deal with the tension between SC hard and OC profit. Management2 adopted *negl* toward franchisee 6 because it expected SC hard and OC profit to be lower in the future. The franchisee would be unwilling and/or unable to adopt the requirements and, since he was of low profitability for the franchisor, the franchisor accepted the franchisee's departure.

Responses subsequent to covo

As pointed out, franchisees 1 to 5 continued with *covo*, while franchisee 6 eventually switched to an exit response.

Responses preceding amloy

Franchisee 7 adopted *amloy* in reaction to SCT2. He had been a very committed franchisee in the past. He had been a member of one of the working groups at the time of SCT1, but he had had a major conflict with management1 that was not really related to SCT1. Nevertheless, the conflict resulted in a betrayal of trust. This franchisee adopted *negl* following the conflict: he did not take action but waited for the management to make amends. Management wanted to do this because it regarded this franchisee as a loyal franchisee who had adopted the proposed changes (SC hard) and had a high profitability (OC profit). The franchisor therefore adopted *covo* and the franchisee switched to *loy*. When SCT2 was introduced, franchisee 7 switched to *amloy* because he was not convinced that the changes would actually take place. The franchisee was very much in agreement with the proposed changes of SCT2, but he was afraid that management2 would not see them through. Therefore, the franchisee waited to see what would really happen under management2 before adopting further responses.

Amloy as initial response

For franchisee 7, the determining variables were:

- OC profit. The franchisee was already satisfied with the profitability of the relationship, but thought he could increase profit if DA was a more uniform organization with an individual identity, a slightly lower positioning, and a higher innovation rate.
- SC hard. This franchisee wanted a higher degree of hardness because he thought a well-known brand name with a certain identity was important. When SCT2 was introduced, he perceived a medium SC hard because he wanted a higher degree of hardness.
- SC pos. This became more important due to the increasing requirements on positioning, and SC pos was very high.
- SC innov. This also became more of a determining factor due to the increasing requirements, and the franchisee considered SC innov as medium: he wanted a higher rate of innovation throughout the DA system.
- OC trust/fd. This became more important due to the increasing requirements, and the franchisee perceived this as medium. Nevertheless, he expected that his degree of trust in another franchisor would be the same as for DA because in his view trust is always an issue between franchisees and the franchisor (as large organization).

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- SC org. This franchisee considered it important for strategic participation to be better organized than in previous years, and he expected this to happen as a result of SCT2.

Because the franchisee was not sure about whether the proposed changes would take place, he was evaluating the alternatives to being a druggist. He considered starting a completely new business. SCT2 prompted this druggist to think about his future and to consider the alternatives, such as doing something completely different.

Management adopted *loy* toward him because it expected the franchisee to sign the FSO, resulting in high SC hard.

Responses subsequent to amloy

At the time of the interview, franchisee 7 was maintaining *amloy* because it was not yet clear whether management2 would persevere with the changes.

Responses preceding negl

Franchisee 8 had been dissatisfied with the relationship for a long time, especially with respect to the increasing degree of hardness and the related cost level. In the past, he had tried to improve the situation through various preceding responses. In sum, over a period of several years, he had shifted from *loy* to *covo* and *agvo* (before SCT2). His initial reaction to SCT2 was *negl*.

Negl as initial response

After the introduction of SCT2, franchisee 8 no longer attended meetings or contacted the franchisor. Nor did he plan to adopt the proposed requirements. He expected that he would eventually be 'thrown out' of the DA system. He had the following determining variables:

- SC hard. For this franchisee, SC hard was very important and he did not want an increasing degree of hardness. There were two reasons why he considered SC hard as important. First, he considered himself as an independent small-business owner who did not want to become too dependent on other parties and who wanted to decide how to run his business. Second, he thought the increasing degree of hardness would result in higher costs, and therefore lower OC profit.
- OC profit. As pointed out, due to the increasing requirements, he expected costs to rise beyond an acceptable level and the profitability of the relationship to be lower.
- OC trust/fd. His perception of OC trust/fd had been low for several decades, but this had never been a problem because management had not really enforced certain requirements in the past. However, since SCT2 had established several requirements, he felt that he would become more dependent on the franchisor and therefore the low OC trust/fd became a problem. Moreover, the low OC profit and OC trust/fd were related: he perceived costs as too high, which he perceived to be partly caused by the fact that the franchisor made too much money at his expense ('unfair dealing').
- SC pos and SC innov. Since positioning and the rate of innovation would be largely obligatory as a result of SCT2, these variables became more important. Since this franchisee perceived low degrees of compatibility for both aspects, he considered this a problem. Additionally, he pointed to the relationship between positioning and the degree of hardness, and between the rate of innovation and degree of hardness.

A lower positioning and a higher rate of innovation would require a higher degree of hardness, which he did not want.

- SC org. He had always perceived a low SC org. However, this only became a determining factor when the requirements were introduced because he wanted to influence the content of the requirements. However, he was against any kind of requirements due to his strong wish for independence, so even a high SC org would not be very important to him.

In sum, the negl franchisee perceived a low strategic and operational compatibility for his determining variables, which resulted in a low level of attractiveness of the relationship. It is interesting that the franchisee adopted negl. It was probably the combination of a lack of attractive alternatives and high switching costs that resulted in negl. The franchisee perceived high switching costs – mainly due to a strong emotional bond with the DA system and the fear of losing his exclusive territory. However, for several years the franchisee had already anticipated a possible break with DA by not prominently displaying the DA name, thus making sure that he build goodwill under his own name instead of DA's. In other words, due to his increased dissatisfaction, he had deliberately kept switching costs low.

The response of the franchisor toward the franchisee had been negl: management2 had not contacted this franchisee for more than a year. However, at the time of the interview, management2 had just contacted him to make an appointment to discuss the future.

Responses subsequent to negl

Some time after the interview, it turned out that this franchisee had indeed left DA and switched to another drugstore system, but it is unclear how this exactly happened. Management2 again had to deal with the tension between SC hard and OC profit. It is highly likely that management2 accepted this departure because it expected a very low SC hard for this franchisee.

Responses preceding agvo

Franchisee 9 had always been a very committed and active franchisee: he had always been involved in various working groups of DA franchisees who had close contact with management. However, he did not agree with the increasing degree of hardness and the increasing costs during SCT2, and he tried to slow down the change process by means of agvo.

Agvo as initial response

His determining variables, in order of importance, were:

- SC hard. For this franchisee, SC hard was also the most important determining variable. He also had two reasons for not wanting a higher degree of hardness. First, he considered it very important to remain an *independent* business owner. Second, he thought the increasing hardness would result in higher costs, and therefore lower OC profit. Given that the franchisees had to finance these costs themselves, he considered it important that they should be at an acceptable level.
- OC profit. As pointed out, this franchisee perceived his profitability as related to the degree of hardness and expected it to become lower in the near future.
- SC pos. This has become a determining factor due to the requirements on positioning. The franchisee perceived SC pos as very high, but simply wanted fewer requirements, and wanted to remain free to decide on his own positioning.

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- SC innov. This had also become a determining factor due to the increased requirements. The franchisee perceived SC innov as medium, mainly because he did not want to be obliged to adopt certain innovations, especially those requiring relatively high investment, which he considered to be risky.
- OC trust/fd. This became more important due to the requirements, and the franchisee perceived this as medium.
- SC org. The franchisee considered this more important due to the increasing requirements. However, he perceived this as low despite the fact that he had been involved in strategic participation. He expected SC org to improve under management2, but in his eyes this did not compensate for the increasing degree of hardness.

His adoption of agvo can be explained by the fact that he actually did not want to leave the DA system, and his agvo was a 'cry for attention'. There were three reasons for this. First, the franchisee thought he could still try to improve his strategic and operational compatibility with the franchisor; he thought he could prevent the increasing degree of hardness and the related higher costs. Second, he perceived the alternatives as very unattractive, and still considered DA to be the best system for his stores. Third, he perceived the cost of switching as high, and related this cost to several factors that he specified (including emotional switching costs), which indicates that he had thought about this carefully.

One additional explanation for the franchisee's agvo was his perception of the way in which the franchisor responded to the franchisees' initial reactions to SCT2. He was shocked that management2 was so willing to let go of franchisees who had been in the DA system for several decades and had helped to make it so powerful. He thought the franchisor's behavior was offensive and that this was not the way to deal with franchisees, which also explains his aggressive response.

Management2's response to franchisee 9's agvo was covo: it attempted to explain why it wanted to introduce certain requirements. However, the franchisee was still not convinced and did not want to adopt the requirements. He did not want to sign the FSO, nor did he want to leave DA.

Subsequent responses to agvo

At the time of the interview, franchisee 9's response was still agvo.

Responses preceding exit

Franchisees 10, 11 and 12 had adopted exit. They did so under very different circumstances, with different determining variables, perceptions of these variables, and preceding responses. Franchisee 10 had switched from loy to amloy before SCT2, and SCT2 prompted him immediately to adopt exit, while franchisees 11 and 12 shifted from loy to amloy and then to covo (before SCT2). They also adopted exit immediately after SCT2 was introduced.

Exit response as the initial response

Franchisee 10 was powerful because he had several DA stores. His determining variables, in order of importance, were:

- OC profit
- Attalt

In sum, franchisee 10 wanted to leave the DA system because he expected that his business would be more profitable if he were completely independent. He thought that the costs of DA were too high, and that he could organize many things himself because of his large number of stores. He therefore considered starting his own franchise system.

Initially, the franchisee perceived switching costs as low, and he decided to leave relatively soon after the introduction of SCT2. He had terminated the contract according to the procedure in the Articles of Association. However, for the franchisor he was an important wholesale customer and a very profitable franchisee. Moreover, the franchisor would lose several locations if this franchisee left the system. The franchisor therefore tried to keep this franchisee by threatening with a lawsuit (agvo response), and suddenly the franchisee perceived his switching costs as very high. As a result, the franchisee adopted covo. The franchise partners eventually worked out their problems and came to an agreement and the franchisee stayed in the DA system.

Franchisees 11 and 12 also differed in their situations. Franchisee 11 owned a very small store that had to deal with strong competition and was performing badly. The franchisee perceived OC profit/cost as very low, and this was the only determining variable because he did not expect to be in a position to meet his financial requirements after SCT2. The franchisee did not consider alternatives: the store was performing too badly to switch to another alternative, and it would probably close down. He also considered the switching costs to be very low. Management was willing to let the franchisee go because the store was performing badly, and it did not expect the franchisee to be able to meet his financial requirements. In other words, OC capa was the franchisor's only determining variable in this case.

Franchisee 12 was in a similar situation to franchisee 6 (who initially adopted covo). Franchisee 6 adopted covo following the introduction of SCT2, but adopted an exit response relatively soon thereafter. Franchisee 12 had already adopted covo before SCT2, and adopted exit very soon after the introduction of SCT2. The main difference between franchisees 12 and 6 was in their timing; their determining variables were the same (OC profit/cost, SC hard, SC pos, SC innov, OC trust/fd, SC org), but it is possible that franchisee 12 had a lower threshold and therefore decided more quickly to adopt an active response. Both franchisees perceived OC profit/cost and SC hard as low and thought these factors were related. According to these franchisees, the high degree of hardness resulted in high costs. As in the case of franchisee 6, the franchisor adopted negl toward franchisee 12.

Because these franchisees felt more or less forced to leave the DA system, they accepted an alternative that they saw as less attractive, namely the UED system. It is interesting to see how this switch from DA to UED influenced the development of the UED system (see Chapter 8, SCT8). The switching costs for these franchisees were low, but the franchisees would still have left DA if the cost of switching had been high.

Summary of determining variables

Table 5.4 presents the determining variables for the different responses.

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Determining variables for franchisees' responses in order of importance					
Covo	Loy	Amloy	Negl	Agvo	Exit
Franchisees 1 to 5 ('voluntary'): OC profit SC hard SC pos SC innov OC trust/fd SC org	-	OC profit SC hard SC pos SC innov OC trust/fd SC org	SC hard OC profit/cost SC pos OC trust/fd SC org	SC hard OC profit/cost SC pos SC innov OC trust/fd SC org	Franchisee 10 ('voluntary'): OC profit Attalt Franchisee 11 ('forced'): OC profit/cost Franchisee 12 ('forced'): OC profit/cost SC hard SC pos SC innov OC trust/fd SC org
Determining variables for franchisor's responses (to franchisees' responses) in order of importance					
Franchisor's response to 1 to 5 = covo ('creating support') Franchisor's response to 6 = negl OC capa SC hard OC profit	-	Franchisor's response to Amloy = loy OC capa SC hard OC profit	Franchisor's response to negl = negl OC capa SC hard OC profit	Franchisor's response to agvo = negl OC capa SC hard OC profit	Franchisor's response to 10 = agvo OC capa SC hard OC profit Franchisor's response to 11: OC capa Franchisor's response to 12 = negl: OC capa SC hard OC profit

Table 5.4 Summary of determining variables for each response type in order of importance for SCT2

5.8 Summary and conclusions for DA and its SCTs

This section will discuss the three types of conclusion that can be derived from the DA case. The section is structured as follows:

- 5.8.1: Conclusions about the independent variables.
- 5.8.2: Conclusions concerning relationships between independent variables and responses.
- 5.8.3: Conclusions about background variables. These variables have not been discussed in earlier sections, but they had an indirect and/or moderating influence on the relationships between the independent variables and the responses.

The conclusions for the two SCTs are discussed together.

5.8.1 Conclusions about the independent variables

This subsection is divided into:

- 1) Independent variables from the franchisees' perspective
- 2) Independent variables from the franchisor's perspective
- 3) The relationship between independent variables

1) Independent variables from the franchisees' perspective

Strategic compatibility

- With respect to strategic compatibility regarding degree of hardness, every DA franchisee had to deal with the tension between the desired degree of hardness and the cost level. DA franchisees differed in the extent to which they considered a well-known brand name to be important, and therefore differed in their desired degree of hardness. Franchisees who did not consider a well-known brand name to be important mostly looked at the cost of participating because they considered their turnover levels to be stable. Other franchisees were willing to invest in certain requirements because they expected these to attract customers and to increase their profitability.
- For SCT1, the low degree of enforcement by management¹ played an important role in the franchisees' perception of strategic compatibility. Because management¹ did not really dare to enforce certain requirements, the franchisees still perceived that they had considerable freedom in running their businesses (e.g. in terms of positioning and rate of innovation). The only requirements for DA franchisees were the promotional activities with the automatically supplied goods, whereby the franchisor aimed to give DA a lower positioning in the market. Because these requirements were about positioning, this sometimes resulted in low SC pos with franchisees, and SC pos therefore became a determining variable for the responses by these franchisees. The same applied at the level of new products with regard to the rate of innovation. For SCT2, it is too soon to tell whether the degree of enforcement actually increased, but franchisees expected aspects such as positioning and rate of innovation to become obligatory, and SC pos and SC innov therefore became determining factors.
- With respect to the rate of innovation, a distinction should be made between strategic compatibility on the three different levels. On the level of new products, the changes were the least radical and involved lower investments than the other business-format adaptations and the business format as a whole. On the level of the general business format, adaptations were the most radical, and franchisees were required to make the highest investment, which often resulted in a low degree of strategic compatibility, according to franchisees. Additionally, these larger investments sometimes resulted in a lower perception of OC profit because a higher rate of innovation would result in higher costs.
- With respect to the franchisees' perceptions of SC org, for both SCTs there was a difference between the franchisees who were involved in strategic participation and those who were not. The franchisees involved in participation often perceived a high SC org, while the franchisees who were not involved perceived this as low. Most DA franchisees had perceived SC org as low for a long time due to the lack of procedures for strategic participation. In the DA case, three types of procedure

turned out to be important: procedures for the selection of franchisees to be involved in strategic participation, procedures for the replacement of these franchisees, and procedures concerning the rights of the Boards.

- With respect to SC growth, there were few problems during SCT1 and SCT2 because growth objectives were not really enforced and there were no problems resulting from duplication.

Operational compatibility

With respect to operational compatibility, the following conclusions can be drawn for the franchisees' perspective:

- OC profit was the most important aspect of operational compatibility for franchisees during both SCTs. The DA case shows that some franchisees focused on cost rather than on their total profitability. This was mainly to do with their perception of a constant turnover level. Because they considered their turnover levels to be constant, these franchisees did not expect extra investment and costs to result in higher profits, and they therefore wanted to keep their costs low. To illustrate this difference, a distinction was made between OC profit/cost and OC profit, although OC profit/cost is simply a variation of OC profit. The reason for this difference can be found in the background variables (see section 5.8.3). In particular, franchisees who perceived weak competitive circumstances considered their turnover to be stable. Additionally, such franchisees often had a small floor area with relatively low turnover, which meant that proportional costs and risk were even higher, and it would take a long time to recoup the investment.
- For OC capa, the following six factors have been distinguished in this study: logistics, automation, communication, information, purchase prices, and general support. The most important issues for discussion during SCT1 were automation, purchase prices, and general support. Together with logistics, they were considered to be the most important of the six factors by the franchisees. During SCT1 there were practical problems concerning these factors, which had cost some franchisees a great deal of money. In these cases, these factors therefore influenced the franchisees' perception of OC profit and OC profit/cost. However, since the factors were not really obligatory during SCT1, only franchisees who 'used' the franchisor's capabilities suffered from this. During SCT2, OC capa became more important for franchisees because they would be obliged to arrange these things via the franchisor, which made the franchisor's capabilities vis-à-vis these aspects more important.
- For OC trust/fd, the following conclusions can be drawn. First, it became clear that a more explicit distinction should be made between trust and fair dealing. Fair dealing is a specific form of trust. It refers to the question of whether the partners perceive the costs and benefits of the relationship to be fairly divided. Trust in general should be seen in broader terms: do the partners feel that the other partner takes their interests into account and will not act opportunistically? With respect to the franchisees' perceptions of trust in general, there was a difference between the franchisees who were involved in strategic participation and those who were not. Those who were involved perceived a high degree of trust, while those who were not generally perceived a lower degree of trust. This applied to both SCT1 and SCT2.

- With respect to OC trust/fd, the DA case shows that a further level of fair dealing can be distinguished in addition to the level distinguished in the research model. This results in two levels of fair dealing:
 - 1) The level of fair dealing between the franchisor and individual franchisees (individual franchise relationships). This level relates to Ring and Van de Ven's concept of fair dealing (Ring and Van de Ven, 1994) and was already included in the research model. It refers to the partners' perceptions as to whether the costs and benefits are shared equally between them. On this first level, several franchisees perceived this to be low during SCT1. There were two reasons for this. First, the use of 'implicit' charges by the franchisor, which the franchisees considered to be non-transparent. Second, the calculation of fees based on turnover. During SCT2, management² aimed to make this more transparent in order to improve the franchisees' perception of fair dealing.
 - 2) The level of fair dealing within the franchise system, as perceived by the franchisees. This refers to the question of whether the franchisees feel that they are treated equally by the franchisor. Due to the lack of procedures for strategic participation, in particular, a large group of franchisees held the perception that certain members of their group received preferential treatment. Several DA franchisees felt that their interests were not taken into account because management and the small group of franchisees involved in strategic participation took only their own interests into account.

Attractiveness of alternatives

An important factor in the franchisees' perception of alternatives during both SCTs was the fact that other franchisors or wholesalers offering franchise-like forms of cooperation began to change their systems in order to attract DA franchisees. These franchisors emphasized a lower degree of hardness and lower cost levels, which would result in higher profitability for the franchisees. It became very clear that individual franchise relationships do not develop in a vacuum. It is interesting to note that there had been some changes in alternatives over time and during SCT2, therefore, alternatives that had not been considered attractive during SCT1 now became so.

Switching costs

- Although this was not explicitly stated in the research model, with respect to switching costs a distinction can be made between financial and contractual switching costs. Financial switching costs refer to the percentage of specific investment and the income resulting from the relationship as a percentage of total income. Contractual switching costs relate mainly to guarantees such as the contract term, minimum purchase quantities, or an exclusive territory. An additional type of switching cost in the DA case is the 'social/emotional' cost. This means that franchisees feel close social and/or emotional bonds with other DA franchisees; leaving DA would be like leaving one's family. Financial and contractual switching costs were mostly low, but several franchisees perceived emotional switching costs as high, particularly during SCT1. It is interesting that emotional switching costs were perceived as lower by several franchisees during SCT2, while financial switching costs had become slightly higher over time for some franchisees who had made specific investments. So, over time there was a change in the type of

switching costs. Because management1 had not really forced franchisees to make specific investments, the cost of switching remained low for many franchisees.

- The research model focuses on switching costs for leaving the DA system, but the costs related to *entering* an alternative system should also be taken into account. In other words, the cost of switching to an alternative was influenced by exit barriers as well as entry barriers to the alternative. There was a relationship between the type of alternative considered attractive and the height of entry barriers. Because other franchisors tried to attract DA franchisees by lowering their entry barriers, it became easier to switch to these alternatives.
- For SCT2, an additional factor played a role for franchisees, namely future switching costs. By signing the FSO, franchisees knew that they would be obliged to make certain investments and that they would be contractually bound to the franchisor for a specified period. For some franchisees, this was a reason to leave because they did not want such restrictions.
- Specific investments did not always lead to switching costs. This became especially clear for SCT2. Some franchisees had already made specific investments in the new DA 2005 format before SCT was actually introduced, but when they left DA in a reaction to SCT2's introduction the franchisor did not force them to remove these from their stores, so this did not constitute an exit barrier for these franchisees. Moreover, entry barriers to alternatives were often also low because the new franchisor did not have requirements relating to store interiors, and accepted the franchisee's existing interior.

2) Independent variables from the franchisor's perspective

Strategic compatibility

- As shown in the timelines for positioning, degree of hardness, rate of innovation, and growth objectives (Figs. 5.3 to 5.5 and 5.6), there was a major discrepancy between what management aimed to achieve and what actually happened. The low degree of enforcement played an important role in this respect. The Articles of the Druggists' Association allowed the management to impose requirements on the DA franchisees, thereby increasing the actual degree of hardness. However, management was reluctant to do this because it was afraid that many DA franchisees would leave. This relates to the most important point of tension for the franchisor under both SCTs: the tension between increasing the actual degree of hardness by imposing and enforcing requirements on the one hand, and, on the other hand, risking the loss of DA franchisees who were an important source of income for the franchisor and who sometimes owned important locations. In other words, during both SCTs, management had to deal with the tension between SC hard and OC profit. Management1 was afraid of losing too many franchisees and therefore did not dare to enforce the proposed requirements, which resulted in a low actual degree of hardness for the DA system. The lack of enforcement had a considerable influence on developments in the other franchise system characteristics and the franchisees' responses within the DA system during SCT1. During SCT2, management2 aimed to be stricter in this regard. However, it is too soon to tell whether management2 has persevered.
- The organization of strategic participation proved to play another role for the franchisor than the other franchise system characteristics. From the franchisor's

perspective, strategic compatibility with individual franchisees on this characteristic was not really important. The organization of strategic participation was merely an instrument for building support for certain requirements among the group of franchisees as a whole.

Operational compatibility

For the franchisor, one necessary condition was that franchisees were able to meet their financial requirements. Therefore, OC capa was always a determining variable. A high profitability in the relationship was desirable, but when the franchisor had only low profits from the relationship, this was still not considered a problem. As pointed out, OC profit became a more important variable when the franchisor wanted to increase the degree of hardness and had to choose between accepting a lower SC hard or losing a very profitable franchisee.

Attractiveness of alternatives

From the franchisor's perspective, the research model distinguishes between two types of alternative for a specific franchisee: finding another franchisee for the location or turning the store into a company-owned store. However, there were difficulties related to this. During SCT1 in particular, most franchisees owned the store premises and could simply continue their drugstores in their own building. The franchisor would therefore lose that location. Moreover, in these situations it was difficult for the franchisor to open a new DA store because the former DA franchisee would still be operating in the area. In sum, the franchisor also had to consider whether he was willing to lose a location if a franchisee did not wish to adopt certain requirements.

Switching costs

Switching costs for the franchisee were generally low. The high switching costs for specific franchisees was largely influenced by their specific wholesaling agreements.

3) Relations between independent variables

Another conclusion that can be drawn for the independent variables is that there were several relationships between independent variables and/or their indicators. These are as follows:

- First, there were indications of relationships between the franchise system characteristics. In the DA case, both SCTs indicated that a lower positioning required a higher degree of hardness, that a higher rate of innovation required a higher degree of hardness, that a higher degree of hardness resulted in more qualitative growth objectives, and that a higher degree of hardness coincided with a higher organization of strategic participation. It is outside the scope of this study to discuss these possible relationships in detail at this point, but Chapter 9 presents a more systematic analysis of possible relationships between the characteristics of the franchise system.
- Second, there were indications of relationships between the actual scores⁴⁴ for three franchise system characteristics (degree of hardness, rate of innovation and growth)

⁴⁴ By 'actual' I mean that these aspects should be *actually* enforced; if the franchisor imposes requirements but does not really enforce them, franchisees can get away with not adopting the requirements and will not have higher cost levels.

on the one hand, and the cost level for franchisees on the other hand. An increase in degree of hardness and rate of innovation, and a change to qualitative growth objectives required greater financial investment by franchisees, thereby increasing their costs and influencing their perceptions of OC profit and OC profit/cost.

- Third, there is a relationship between the actual degree of hardness and high switching costs. An increase in the actual degree of hardness often required more specific investments by franchisees, thereby increasing the financial cost of switching. During SCT1, this did not occur because there was a low degree of enforcement and the franchisees were not obliged to make specific investments. As pointed out, for SCT2, the franchisees who signed the FSO were supposed to make specific investments and increase their contractual bonds, which they then took into account as 'future switching costs'.
- The relationship between involvement in strategic participation and the degree of trust has already been pointed out in the text: franchisees who were involved in strategic participation perceived a higher OC trust/fd than those who were not.
- There was a relationship between the type of alternative that was considered attractive and the level of switching costs. A softer system required fewer specific investments from franchisees, and therefore had lower entry barriers than a hard alternative system. As pointed out, it is interesting that, during SCT1, the ETOS management lowered the entry barriers to ETOS by lowering its degree of hardness.

5.8.2 Conclusions concerning relationships between independent variables and responses

This section consists of two subsections:

- 1) Conclusions from the franchisees' perspective
- 2) Conclusions from the franchisor's perspective

1) Conclusions from the franchisees' perspective

This subsection consists of two parts:

- Conclusions about the responses themselves
- Conclusions about the relationship between responses and independent variables

Conclusions about the responses themselves

The responses during both SCTs were more heterogeneous than currently assumed in the literature. This response heterogeneity became particularly clear for the franchisees. As can be seen from Tables 5.2 and 5.4, the responses of the franchisor were more 'stable'; they were mostly passive responses. The franchisor adopted an active response only when he really was afraid of losing a franchisee. Based on the DA case, four conclusions can be drawn about the current typology of responses as presented in Chapter 3.

- First, an additional response should be added to the passive responses, namely the 'ambiguous loyalty' response (amloy). Amloy is less destructive than negl and less constructive than loy. This response involves waiting to see what happens before adopting further responses. This turned out to be a 'dangerous' response because it was not apparent to the management, and a number of franchisees who adopted this response quickly shifted to exit, which was unexpected for the management.

- Second, franchisees adopting covo had different motives for this. Some adopted covo because they felt 'forced' to do so. They felt that the relationship with the franchisor would deteriorate if they did not adopt this response. This would result in an undesirable situation. This type of covo can be termed as 'forced covo' (franchisee 6 for SCT2). By contrast, other franchisees adopted covo because they agreed with the management's plans but wanted to be actively involved in discussing future possibilities. The response of these franchisees can be seen as 'voluntary covo' (franchisees 1 to 5 for both SCTs). These franchisees often had close personal contacts with management and in turn were 'used' by the management to build support among the larger group of franchisees.
- Third, the forced/voluntary distinction can also be made for the exit response. Several franchisees adopted exit because they felt forced to do so. They felt that, if they stayed, an unbearable situation would arise. A number of other franchisees did not really feel forced to leave, but were 'pulled' toward what they perceived to be a more attractive opportunity. In both SCTs, it turned out that franchisees adopting forced exit often switched to a 'lesser' alternative.
- Fourth, with respect to exit, a distinction should be made between leaving the franchise system and leaving the relationship. In some cases, DA franchisees left DA but entered STIP, thereby remaining in a relationship with the same franchisor. In other cases, the franchisee wanted nothing more to do with the franchisor, and left the franchise system and the relationship. The latter case resulted in higher losses for the franchisor because all links ceased to exist.

Relationship between responses and independent variables

As shown in Tables 5.2 and 5.4, the determining variables were different for each response. When comparing the determining variables in the responses and in both tables, the following conclusions can be drawn from the franchisees' perspective:

- First, the voluntary-covo and loy franchisees had the same determining variables (in Table 5.2). The voluntary-covo franchisees wanted the scores for the franchise system characteristics to change relatively soon, so they adopted an active response toward the franchisor in order to achieve that. The loy franchisees agreed with the changes and therefore did not feel the need to contact the franchisor. These franchisees looked at OC profit rather than OC profit/cost because they believed they could increase their turnover and profitability by adopting certain requirements.
- Second, the amloy, negl and forced-exit franchisees had the same determining variables during SCT1, but their thresholds for these variables differed. Once a franchisee's threshold was reached, or the franchisee expected it to be reached soon, he switched from a passive response to an active response toward the franchisor. The amloy and negl franchisees had not yet reached their thresholds. The difference in thresholds can be explained by background variables (see section 5.8.3). It is interesting that, for these franchisees, SC org and OC trust/fd became more important when additional requirements were introduced. This can be explained by the fact that, due to a higher degree of hardness (perceived by the franchisee), the franchisee felt more dependent on the franchisor. As a result of this perceived dependency, OC trust/fd suddenly became more important for the franchisee. The same applied to SC org; this was not considered important until franchisees perceived that the actual degree of hardness – and therefore their

dependence – had increased, and they wanted to have greater influence on the requirements through more efficiently organized strategic participation. For agvo, the order of determining variables was slightly different: SC hard was the most important variable. This franchisee considered it very important to be an independent small-business owner, and therefore did not want a high degree of hardness at all. This strong desire for independence turned out to be one of the background variables (see 5.8.3).

- In Table 5.4, the voluntary-covo response and the amloy response had the same determining variables. These franchisees had the same aims as the franchisor, but differed in their expectations for the future. The voluntary-covo franchisees believed that their future perceptions of the determining variables would improve, while the amloy franchisee was less sure about this. One additional difference between Table 5.2 and Table 5.4 is in the determining variables for the amloy response. For SCT1, the determining variables were OC profit/cost, SC hard and SC pos. The determining variables for amloy responses during SCT2 were SC hard, SC pos, SC innov and attalt (the attractiveness of alternatives). In other words, the motives for amloy varied considerably.

In sum, the DA case showed that the following aspects were important in understanding why a franchisee adopted a certain response at a certain point in time:

- The franchisee's determining variables at the time, in other words, which variables did the franchisee consider as important in the relationship at that point in time. These determining variables were influenced by several background variables (see section 5.8.3). The determining variables mostly related to strategic and operational compatibility. On the basis of these variables, the partners evaluated the attractiveness of their current relationship. If the level of attractiveness was high, the partners did not evaluate alternatives or switching costs; these were not evaluated until the current relationship became unattractive. Additionally, there was an order of priority for alternatives and switching costs. First, alternatives were evaluated. When an attractive alternative was available, high switching costs became less important. Moreover, in several situations the current relationship was so unattractive that the franchisee accepted an alternative that was not so attractive but which was better than the current relationship.
- The franchisee's perceptions of the determining variables at the time. These perceptions were influenced by several background variables (see section 5.8.3).
- The franchisee's thresholds for the determining variables. A 'threshold' indicates that the franchisee accepted a certain level or degree of strategic or operational compatibility. Once that level had been reached, the franchisee adopted another response to deal with this, and in most cases this was an active response.
- The franchisee's expectations for future developments in his determining variables. It became clear that differences between the franchise partners' desired scores indeed played a role in the adoption of responses during SCT1 and SCT2, because it influenced the partners' expectations of the future situation. For example, a franchisee might perceive a medium or high SC hard at a certain point in time, but he might expect it to be lower in the near future due to a different desired score by the franchisor. It turned out that this also influenced franchisees' responses.

Moreover, it has become clear that the franchisees switched between responses during the SCTs. These response switches were always caused by certain triggers. In the case of DA franchisees, the triggers were the following:

- Changes in franchise system characteristics, which resulted in changes in franchisees' perceptions of strategic compatibility. In the DA case, the changes in positioning and the level of hardness were the underlying factors for most response switches.
- Changes in one of the other independent variables: OC capa, OC profit, OC trust/fd. In both SCTs, the most important were changes in OC profit. When franchisees expected a lower OC profit (or OC profit/cost), they often adopted an active response. It is interesting that several DA franchisees had perceived OC trust/fd as low for a long time, but this only resulted in certain responses when the degree of hardness increased (see below).
- Responses of the franchisor. Franchisees adapted their own responses to the responses of the franchisor. In several situations, the DA franchisee perceived a passive response by the franchisor when they wanted to discuss their issues, and therefore adopted an exit response in return.

It also becomes clear from Tables 5.2 and 5.4 that the responses had different 'hierarchies' of determining variables. OC profit (or OC profit/cost) played a role in every response type. In addition, SC hard, SC pos and SC innov were determinant in almost every response type, but their order of priority varies. The most important variables for covo and loy were SC hard and OC profit. For the amloy, negl, agvo and forced-exit responses, OC profit/cost was most important during SCT1. These franchisees did not want extra costs because they considered their turnover levels to be stable, while the other franchisees expected to improve their profitability with an increasing degree of hardness. In SCT2, SC hard was the most important determining variable for the negl and agvo franchisees, for whom the degree of hardness meant not only an increase in cost level, but also constituted a threat to their independent status. One explanation for this is that the different responses were adopted by different 'types' of franchisees (background variable, see section 5.8.3).

2) Conclusions from the franchisor's perspective

As pointed out, the franchisor's responses were relatively stable compared to the franchisees' responses. The franchisees' ability to fulfill their financial requirements (OC capa) was an essential condition, and was therefore always a determining variable. The additional determining variables for the franchisor were mostly the same: SC hard and OC profit (see Tables 5.2 and 5.4). Before SCT1 in particular, it did not matter to the franchisor whether a specific franchise relationship was very profitable or hardly profitable at all. As long as it was profitable, and the franchisee met his financial requirements, there was no problem. However, when management wanted to increase the degree of hardness, tension arose between the need to impose and enforce requirements and the risk of losing profitable franchisees. The higher the desired degree of hardness and profitability from the franchisee for the franchisor, the greater the tension, particularly if a very profitable franchisee would not want to adopt certain requirements. During SCT2, the introduction and enforcement of requirements became more important for the franchisor. The franchisor adopted loy when he expected that a franchisee would be willing and able to comply with the increasing requirements. The franchisor mostly adopted negl to the less cooperative franchisees, and expected that they would decide to leave. During SCT2,

management expected to adopt exit responses toward franchisees who did not wish to adopt the FSO and the resulting requirements. It is interesting to note that management adopted covo only toward those franchisees who it thought could help to build support among the larger group of franchisees, or when the franchisor did not want to lose specific franchisees.

5.8.3 Conclusions about background variables

This section consists of two parts:

- 1) Background variables from the franchisees' perspective
- 2) Background variables from the franchisor's perspective

1) Background variables from the franchisees' perspective

From the franchisees' perspective, four groups of background variables proved to be relevant during the SCTs of DA. The groups are as followings:

- Store characteristics.
- Franchisee characteristics.
- Franchisor/managerial characteristics.
- Characteristics of the franchise system.

These four groups, in turn, consist of other variables, which are discussed below.

Store characteristics.

- Location characteristics. These relate to the store's location and its competitive circumstances, or at least to the franchisees' perceptions of those circumstances. They influenced the franchisees' desired scores for certain franchise system characteristics, and thereby indirectly influenced the franchisees' perception of strategic compatibility with the franchisor. The location characteristics determined whether franchisees saw their turnover as stable, or whether they had the impression that they could attract more customers and increase their profitability through increased investment. In the DA case, several franchisees were located in villages and considered a well-known brand name (and high degree of hardness) to be unnecessary because they regarded their turnover as stable.
- Store performance. This is also a background variable: when a store was performing well, the franchisee did not really see the need to change. Due to the favorable economic situation before and during SCT1, drugstores in general had been performing well, and several franchisees perceived that customers would come to their stores anyway. Consequently, they did not find it necessary to make extra investments. During SCT2, economic conditions were unfavorable, and franchisees were hesitant to make large investments because they were not sure whether they could recoup this investment over a reasonable time period.

Franchisee characteristics

The following background variables can be distinguished for franchisee characteristics:

- Personal/psychological characteristics. For several DA franchisees, SC hard was the most important variable, particularly when the degree of hardness was higher than they thought necessary. These franchisees considered their independence as small-business owners to be very important, and therefore disagreed with a certain level

of hardness. On the other hand, other franchisees wanted a higher degree of hardness and regarded independence as relatively less important because they expected higher profits from a well-known brand name. This difference in the desire for independence had an indirect effect on the franchisees' responses. Franchisees with a strong desire for autonomy objected to a high degree of hardness, and often adopted a destructive response.

- The 'history' of the franchisee. This relates to the previous experiences of the franchisee. The 'traditional' characteristics of the DA system, particularly with regard to hardness and positioning, were especially valued by older franchisees who had been with DA for several decades. These franchisees wanted to maintain a low degree of hardness and a high positioning. During SCT1 in particular, some franchisees considered that promotional activities were incompatible with their identity as druggists. Moreover, several franchisees had taken over the DA store from their parents and had grown up with DA. This greatly influenced their perception of switching costs due to their social/emotional bond with DA.
- Membership of the Franchise Board (Board of Participants). As previously mentioned, a franchisee's membership influenced OC trust/fd: members of the Franchise Board often had a higher OC trust/fd than non-members. Moreover, because the members were in close contact with management, management could convince them more easily of the need for certain changes, which probably resulted in greater strategic compatibility for certain franchise system characteristics.

Franchisor/managerial characteristics.

- Management style. This can be characterized as 'authoritarian' as opposed to 'participative'. Some DA franchisees perceived management's style as authoritarian, which resulted in a low OC trust/fd. Moreover, some franchisees did not like the authoritarian way in which management introduced SCT2, and this influenced their perception of the actual degree of hardness. Due to the authoritarian style, these franchisees perceived a high degree of hardness, which influenced their perception of SC hard.
- Management history. The CEO during SCT1 had come from the ETOS system, which at that time consisted mainly of company-owned units with only a few franchised units. The DA franchisees were afraid that the CEO wanted to manage the DA system as if it consisted of company-owned units and therefore would not take the franchisees' interests into account. Another manager had been involved in the introduction of 'business-format thinking' at a well-known supermarket chain, and the DA franchisees expected that he would try to do the same at DA. In sum, the history of the management led the franchisees to form certain expectations about the objectives of the managers and their management style.

Characteristics of the franchise system.

- History of the system. The Druggists' Association had always been owned by its members (the DA franchisees). Because the DA franchisees owned the DA system, they were very skeptical that a management team from 'outside' should be managing DA. Moreover, because the DA franchisees indirectly paid the salaries of the managers (via their membership of the Druggists Association), they felt that the management should not be able to impose requirements on them.

2) Background variables from the franchisor's perspective

The background variables from the franchisor's perspective consist of one background variable, namely 'managerial characteristics'. The following managerial characteristics have been identified:

- Management's experiences with previous strategies in other organizations. This had an indirect and moderating effect because it influenced what management saw as viable strategies for the DA system and the way in which the strategies should be implemented. They had been involved in the management of harder systems or in the same kind of change trajectories at other organizations. Due to their previous experience, they expected the changes at DA to take only a few years. However, they found out that this was not the case after they introduced their SCTs.
- Personal characteristics of the managers. The members of the management team had certain personal characteristics that indirectly influenced their management style and the way in which they responded to franchisees.