

## The Roles of Trust in Franchising Relationship: The Malaysian Franchisees' Perspectives

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**Abstract:** Franchising has become an extremely popular trend in most countries in the world when a company wishes to expand their business operations in either domestic or international markets. Franchising allows for rapid and effective market penetration using franchisee resources such as financial capital, managerial talents and local market knowledge. This study attempts to examine empirically relational value which may influence the trust in franchising relationship from franchisee's perspective. Furthermore, this study examines the effect of trust towards loyalty in franchising relationships. This study adopts a quantitative approach, applying a cross-sectional study. Thirteen franchisors were willing to participate in the survey and one hundred and twenty eight useable questionnaires were received from mail and online survey from franchisees. The results provide strong evidence that franchisee's trust is found to significantly affect franchisee's loyalty to stay in the franchise system. The inclusion of relationship value is suggested to contribute additionally to the literature of relationship marketing relationship and provide a more complete model within the franchising context. Findings also imply the need for franchise players in general and franchisors in particular, to strategically handle the key antecedents of trust and loyalty in pursuit of a more competitive and long term profit.

**Key words:** Franchising • Trust • Relationship quality • Loyalty

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### INTRODUCTION

There has been a major shift in ensuring the existence of an organization in its business life-cycle, especially in open markets. Paradigm shifts in business organization are needed in order for businesses to improve their market share and expand into new ventures. Firms have options to develop new business models such as franchising and licensing; these can be imitated and work in diverse economic systems and different geographical areas. Nevertheless, franchising is found to be the best option to enter for a new market either local or international markets [1]. Frank and Stanworth [2] argue that franchising is becoming more important in generating national economies and has attracted the interest of scholars, researchers, journalists, politicians, etc. in exploring the uniqueness of the franchise system.

Furthermore, franchising allows for rapid and effective market penetration using franchisee resources such as financial capital, managerial talents and local market knowledge[3]. For example, the US Sewing

Machine Company, Singer, has successfully used franchising of its business by appointing enterprises to distribute its products and provide continuing customer support throughout the US market [3]. The franchise model has proven to be an effective business model. McDonald, one of the largest franchised fast-food restaurants in the world was established in 1955 and successfully ventured into over 119 countries across 35, 000 outlets [4]. Others chains such as McDonald's Restaurants, Holiday Inns, Burger King, Dunkin' Donuts, Pizza Hut, Subway, KFC and Kenny Rogers Roasters also use franchise systems [5]. Despite the importance of value in the marketing discipline, research on customer value in B2B markets is still under-researched and is conducted at a conceptual level [6, 7].

Relationship value (RV) is found to be a new research area and the measurement of value in a buyer-seller relationship is still an under-researched concept[8]. Furthermore, superior value provided by a firm is considered the key in creating and sustaining long-term buyer-seller relationships in B2B markets [9].

In the marketing literature, many research studies focus on service quality and relationship marketing, while research dealing with relationship quality is scarce [10], [11]. The development of the B2B relationship is crucial due to extensive customization and the long-term relationship with customers [12]. However, there is limited research on the application of RQ from a franchising context [13-16].

Therefore, this study focuses on the franchisor-franchisee relationship quality mainly trust which is considered an important element in maintaining the franchising venture success over the long term. Additionally, Clarkin & Rosa [17] highlight that the relationship quality between inter-firms parties ultimately determines the success of a franchise business. In the relationship quality (RQ) studies, there is a lack of consensus on the dimensions of RQ, though there is consensus that relationship quality is a higher order construct consisting of several distinct, but related dimensions [18]. In this study, the researchers have identified trust as the main construct of RQ in franchising relationship. The study also examined the effect of relationship value and RQ towards loyalty from the perspective of franchisees in Malaysia context.

### **Literature Review**

**Relationship Value:** Relationship value has become more important since the transmission shift from transactional to relational marketing orientation [19][63][64]. Ulaga [8] highlighted that the concept of relationship value is rooted in business and service marketing. Eggert & Ulaga [6] define value from the industrial marketing perspective as the trade-off between benefits and sacrifices of a supplier's offering, as perceived by key decision-makers in the customer's organization and taking into consideration the available alternative suppliers' offering in a specific use situation.

In franchising, the customer who perceives value is the franchisee (as a buyer) who purchases the rights from the franchisor (seller) to operate the business in the franchise system. Meanwhile, franchisor who is the owner of trademark/business system will transfer the knowledge to franchisee and expect them to perform the business operating procedures and paying franchise fees as a continuity business supports by franchisor. The franchisee has made a huge investment (monetary and non-monetary) in the franchise business such as paying the franchising fees, initial set-up costs, etc. and looking for future success or profitability in the long term. The

franchisee perceived relationship benefits refer to franchisor products, brand, support service, standard operating procedures (SOP), training, marketing collaboration and other support as stipulated in the franchise agreement which refers to franchisor obligations. Moreover, the intrinsic trade-off between the value derived by the franchisee and the franchisor is considered an important driver in the relational exchange [20].

**The Relationship Quality:** RQ is an important aspect in maintaining inter-firm relationships and is considered the essence of relationship marketing [21]. The concept of RQ is rooted in the field of relational marketing (RM) [22], [23]. The key aspects of RM are important not only in gaining customers and creating transactions but also in maintaining and ensuring continual relationships [24]. RQ is an important aspect in maintaining inter-firm relationships and is considered the essence of relationship marketing [21]. The high quality of relationships between firms will bind the relationship together (e.g. buyer-seller, franchisor-franchisee) and will create more stable exchange of goods and currency in the long term [25], [26]. RQ is defined as "the customer is able to rely on the salesperson's integrity and has confidence in the salesperson's future performance because the level of past experience has been consistently satisfactory" [22]. There is no commonly used or consensus of definition of RQ in the business-to-business context. There is no consensus in the literature on the set of dimensions that represents the construct of RQ [10], [27]. Many studies related to RQ employ different dimensions in various research contexts and business settings. In franchising, Modell [28] highlighted that trust is considered as a key factor to of successful franchise relationship. Furthermore, trust in franchising is function as the bond to strengthen the relationship between franchisor and franchisee for mutually cooperation in business operations. Therefore, this study is employed trust as main constructs of RQ which predicted as main a key factor for franchisor-franchisee relationship success.

**Trust:** Trust is considered an important dimension that contributes to positive outcomes and improves the confidence level in any relationship involving two parties. In franchising, Dickey, McKnight and George [29] and Chiou, Hsieh & Yang [14] have used trust as a major construct of RQ in their study, meanwhile Bordonaba-Juste & Polo-Redondo [13] conceptualize RQ as the long

term relationship which is characterized by high levels of trust and commitment. Ishak & Jantan [30] also find, in their meta-analysis, that most cited studies in RQ are identified as trust as core dimensions of RQ. As align with Bordonaba-Juste & Polo-Redondo [31] the researchers will include trust as the main constructs in franchisor and franchisee RQ.

Trust has generally been described through two different components, namely; trust in the partner's *credibility* (or honesty/integrity) and trust in the partner's *benevolence* [32], [33]. Credibility refers to the extent to which one partner believes that the other has the required expertise to perform the job effectively and reliably; while, benevolence refers to the extent that one partner believes that its counterpart has intentions and motives that are beneficial to the former when new conditions arise [16]. Bordonaba-Juste and Polo-Redondo[31] also support the importance of trust in the franchisor-franchisee relationship. They find that franchisee's trust in their franchisor influences their levels of satisfaction and intention to continue to a greater extent in short-term relationships.

**Loyalty:** The concept of customer loyalty is frequently seen as an expected outcome of relationship marketing activities[34]. Moreover, loyalty marketing is used interchangeably with relationship marketing [35][65][66]. The loyalty concept has become an important factor in sustaining a firm's competitive advantage [36][67][69][70]. According to Rauyrue and Miller [37], the concept of loyalty was not widely studied from the business-to-business perspective compared with the consumer context and the service market. The importance of loyalty in B2B is supported by researchers who use several constructs that reflect the key aspect of retention (loyalty) in long-term relationships such as relationship continuity, long-term orientation, repurchase intention, intention to continue, commitment, attitudinal loyalty and loyalty intention [13], [22], [23], [32], [34], [38], [67], [68], [69]. In franchise businesses, loyalty is applicable for the franchisor and franchisee who continue to remain in the business.

**Hypotheses Development:** Ulaga and Eggert [39] found that relationship value is positively correlated with trust, commitment and satisfaction among senior purchasing managers (buyers) towards their supplier in US manufacturing industries. Moliner [40] highlights that perceived value is identified as important in the formation

of benevolence and honesty (trust dimensions). In the marketing field, loyalty is widely recognized as an important construct producing greater collaboration, fewer complaints and greater profitability from the customer[41], [42]. In the context of business-to-business, loyalty is a key variable for studying long term relationships between firms [41]. De Wulf, Odekerken-Schroder, & Iacobucci [43] found that the higher level of trust and commitment will lead to a higher level of behavioral loyalty. Furthermore, Auh and Shih [44] highlight in their findings that the better the relationship quality a customer has with the vendor will result in greater customer loyalty. Based on the above discussion, the following hypothesis is generated:

- H1: There is a positive relationship between relationship value and franchisor's credibility
- H2: There is positive relationship between relational value and franchisor's benevolence.
- H3: There is a positive relationship between franchisor's credibility and loyalty.
- H4: There is positive relationship between franchisor's benevolence and loyalty.

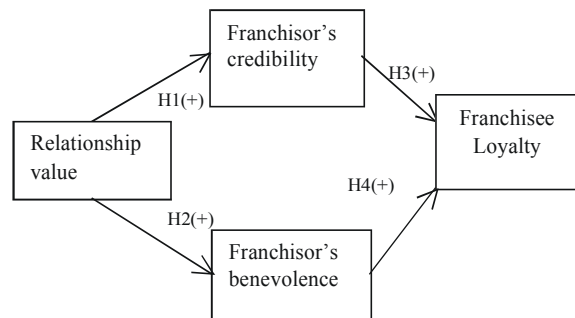


Fig. 1: Theoretical Framework

## MATERIALS AND METHODS

This study focuses on the Malaysian franchise system and will exclude foreign franchise businesses from the research sampling. The respondents are franchisees who operated franchise business in Malaysia. This study is based on a quantitative approach, applying a cross-sectional study. A total of 400 questionnaires were distributed and 133 questionnaires were successfully returned. The usable response rate was 32 percent comprising 128 usable responses from a total of 400 questionnaires sent to franchisees. The questionnaire consists of three main sections, namely: Section 1 detailing the franchisee's background data; Section 2 to

measures the franchisee’s relationship value and trust, whereas Section 3 to measures franchisees’ loyalty. The relationship value is measured by six item scales which indicate the respondents’ perception of the overall evaluation of comparable value derived from relationship benefits and sacrifices. The constructs of relationship value was adapted from Ulaga & Eggert [45]. Trust was measured by six items and commitment was measured by seven items. Trust items are adopted from various studies such as [32], [46], [47]. Franchisee loyalty was measured by two items each for behavioral and attitudinal loyalty. Four items of franchisee loyalty were adapted from Gilliland and Bello [48]. Most questions in Section 2 and 3 are mainly in a 5-point Likert Scale, while category and dichotomous scale was used widely in Section 1. All studied items were identified as reflective measurements

**RESULTS**

The measurement and structural model were tested by using structural equation modelling. The study uses SmartPLS software version 2.0 M3 in order to evaluate the validation of measurement scales and to test all hypotheses proposed [49]. PLS is used when ordinary assumptions such as multivariate normality and large sample size are not met. PLS is a statistical tool specifically designed to cope with small datasets, missing values and the presence of multi-collinearity often exists in samples used in marketing research [50].

In order to proceed with SEM-PLS, there are two stages for performing SEM which consist of a measurement model and structural model [51], [52]. Firstly, the measurement model is evaluated by checking the reliability and validity of each measure used in the framework model. The composite reliability and internal consistency reliability (Cronbach’s alpha) are evaluated to ensure each value follows the recommended evaluations. The cut-off value for composite reliability and internal consistency reliability (Cronbach’s alpha) is 0.7 [53-55]. After all measurement of all constructs have adequate reliability and validity assessment, all the measurement items are kept for testing the structure model. As tabulated in Table 1, the AVE of all latent constructs ranges from 0.650 to 0.795, which exceeds the recommended level of 0.50 [56].

For discriminant validity, the square roots of AVE for each construct as presented in Table 2 are less than the AVE latent variables. In conclusion, the measurement model demonstrates adequate convergent validity and

discriminant validity. between the construct and the other constructs [57]. In statistically term, the squared root of each construct’s AVE should be greater than its highest correlation with any other construct in measurement model [58]. As shown in Table 2, the squared roots of the AVE latent variables are greater than the correlations for each construct.

For hypothesis testing, the path analysis was used to verify all hypotheses generated in this study, the PLS software generates estimates of standardized regression coefficients which refer to beta values for model path [59]. PLS uses re-sampling procedures known as nonparametric bootstrapping to evaluate the significance of the parameter estimates [60]. In this study, the researcher uses 5000 resampling procedures for bootstrapping as aligned with previous studies in the business-to-business context [52].

The results of the model estimation including standardized path coefficient, one-tailed significance (1.65) of the paths are presented in Figure 2. Based on Table 3, the results of hypothesis testing show that all hypotheses are at significance levels of  $p < 0.05$ . Relationship value is positively related to franchisor’s credibility, whereas franchisor’s credibility is positively related to franchisee’s loyalty. Moreover, relationship value has positively related to franchisor’s benevolence and it’s positively related to loyalty. Therefore, all hypotheses in this study; H1, H2, H3 and H4 are accepted. Overall, this model is explained 47% of variance in franchisee’s loyalty.

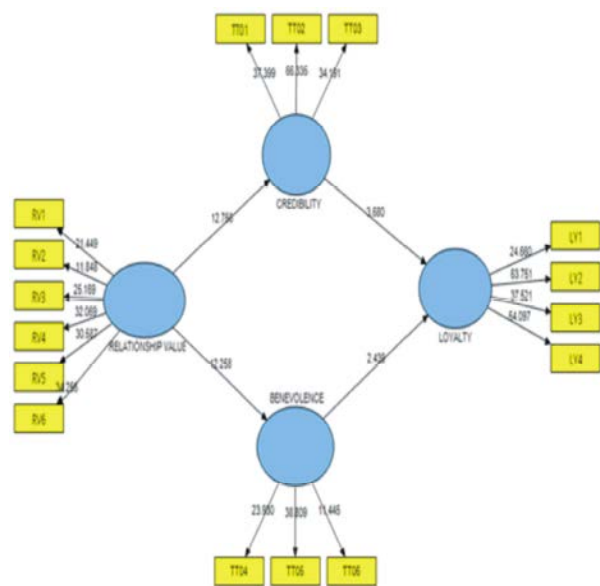


Fig. 2: Results of the path analysis

Table 1: Measurement Model

| Constructs         | Items | Loadings | CR <sup>a</sup> | AVE <sup>b</sup> |
|--------------------|-------|----------|-----------------|------------------|
| Loyalty            | LY1   | 0.832    | 0.936           | 0.784            |
|                    | LY2   | 0.917    |                 |                  |
|                    | LY3   | 0.883    |                 |                  |
|                    | LY4   | 0.908    |                 |                  |
| Relationship Value | RV1   | 0.802    | 0.917           | 0.650            |
|                    | RV2   | 0.672    |                 |                  |
|                    | RV3   | 0.806    |                 |                  |
|                    | RV4   | 0.845    |                 |                  |
|                    | RV5   | 0.845    |                 |                  |
|                    | RV6   | 0.852    |                 |                  |
| Trust              | TT01  | 0.887    | 0.921           | 0.795            |
|                    | TT02  | 0.915    |                 |                  |
| Credibility        | TT03  | 0.872    | 0.852           | 0.658            |
|                    | TT04  | 0.814    |                 |                  |
| Benevolence        | TT05  | 0.870    | 0.852           | 0.658            |
|                    | TT06  | 0.745    |                 |                  |

<sup>a</sup> Composite reliability (CR) = (square of the summation of the factor loadings)/{(square of the summation of the factor loadings) + (square of the summation of the error variances)}

<sup>b</sup> Average variance extracted (AVE) = (summation of the square of the factor loadings)/{(summation of the square of the factor loadings) + (summation of the error variances)}

Table 2: Discriminant validity of constructs

| Construct          | Benevolence | Credibility | Loyalty | Relationship value |
|--------------------|-------------|-------------|---------|--------------------|
| Benevolence        | 0.811       |             |         |                    |
| Credibility        | 0.789       | 0.892       |         |                    |
| Loyalty            | 0.631       | 0.663       | 0.886   |                    |
| Relationship value | 0.661       | 0.659       | 0.683   | 0.806              |

Note: The square root of AVE values is shown on the diagonals and printed with bold; non-diagonal elements are the latent variable correlations

Table 3: Path coefficient and Hypotheses testing

| Relationship                      | Coefficient (B) | T-value  | Result    |
|-----------------------------------|-----------------|----------|-----------|
| Relationship value -> credibility | 0.659           | 12.756** | Supported |
| Relationship value -> benevolence | 0.661           | 12.258** | Supported |
| Credibility -> loyalty            | 0.437           | 3.680**  | Supported |
| Benevolence -> loyalty            | 0.287           | 2.439**  | Supported |

Note: \*\*Significant at p<0.05 based on one tail t-statistic table, as t-value greater than 1.65.

### DISCUSSIONS

The positive relationship between relationship value and trust reflects that the higher the relationship value of the franchisee, the higher they tend to perceive themselves to be higher in trust. The positive relationship between relationship value and trust indicates that franchisees really recognize all valuable benefits received from the franchisor (such as training, services support, market analysis assistance, software support) over their investment in the franchise business. This suggests that when franchisors invest time and efforts to ensure that

they are together with their franchisees, that they are more trusted by their franchisees. Therefore, franchisors shall look into the investment values (benefits - gives and gets components) received by franchisee in maintaining good relationship quality. Moreover, the finding suggests that franchisor's credibility and franchisor's benevolence are important indicators of RQ in franchise relationships. Therefore, this findings are aligned with previous findings in which most of researchers in relationship marketing argued that trust is important indicators to measure RQ especially in business-to-business context [9], [61], [62]. Therefore in the franchising context, the development of trust is important to establish a successful relationship. The positive relationship between trust and loyalty in this study reflects that franchisees with high levels of trust will stay loyal in the franchise system and contributes to a positive performance. Indeed, the higher level of trust in franchisees, the more likely they are to stay in relationship.

### CONCLUSION

Our study is contributed advances in franchise knowledge. Specially, it's showed that the relational value, trust and loyalty are inter-related in franchising relationship. Relationship value is important criteria in ensuring all benefits are received well by franchisees. Relationship value seems to become a mechanism for franchisees to evaluate the episode benefits / relationship benefits over episode/relationship sacrifice. Based on franchise investment (monetary and non-monetary) in the franchise system, franchisees will appreciate the support and assistance offered by franchisors in ensuring their franchise business success over the long term. Furthermore, trust is identified as important factor in ensuring the franchisee's to stay loyalty in franchise business. The existence of trust in franchise relationships will reduce transaction costs (monitoring costs) and lead to higher commitment in the franchise relationship. Trust is built in franchise relationships through the experiential interaction and communication between franchisor-franchisee whereas building and retaining trust is important to a successful franchise relationship. Future study is fully recommended to replicate this model in other business-to-business models such as importer-exporter, supplier-manufacturer, wholesaler-retailer etc. By considering existing research limitations, more effort for subsequent research is needed in identifying other antecedents and outcomes of RQ especially from the franchising perspective.

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