

## **Relationship value, relationship quality and loyalty among Malaysian franchisees**

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### **Abstract**

Franchising is an increasingly popular way of conducting and expanding business in the global environment. In a franchising business, the franchising relationship quality (RQ) is considered important in ensuring success, since franchisors-franchisees are considered as business partner. Studies on franchisee-franchisor relationships from the franchise perspectives are very important and there has been a lack of research on the franchisee motivations for entering into the relationship mainly from Malaysia context. Therefore, this study will attempt to examine the relationship between relationship value (RV), RQ and loyalty among Malaysian franchisees. A total of 400 questionnaires were mailed by using random sample to a local-home grown franchisee. The result of this study expects to develop an understanding of relationship quality among Malaysian local home grown franchisees. This study also contributes to the field of relationship marketing especially in managing business-to-business relationship.

**Keywords:** relationship value, relationship quality, franchisee, loyalty.

### **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 extend 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 entry for a new market in either local or international markets (Quinn & Doherty, 2000). Frank and Stanworth (2003) 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 (Stanworth & Curran, 1999).

In Malaysia, the government has implemented many programs and activities in order to cultivate more franchisors and franchisees to be involved in franchise business. The Franchise Development Division, Ministry of Domestic Trade, Cooperatives and Consumerism plan and implements franchise development policies, initiatives and programs in order to promote franchise development in Malaysia. Furthermore, the primary government agency, led by Permodalan Nasional Berhad (PNS), plays an important role in developing strategies and implementing many programs to develop successful franchisees and franchisors in Malaysia. The strong support from the Malaysian government in cultivating franchising has produced popular local home-grown franchisors such as Marrybrown, Secret Recipe, Nelson's, D'Tandoor and Smart Reader Worldwide. They have successfully expanded businesses locally and internationally. Franchising has and continues to contribute to Malaysia's economy by generating and replicating successful businesses to a franchise-oriented system.

This paper is structured as follows. It addresses the relationship quality (RQ) constructs in franchising relationships. This then entails the issues of "what are the dimensions used in operationalizing the concept of RQ in franchising perceptively?" Secondly, we will discuss "What are the effects of RQ towards loyalty?" Thus, this study will explore the outcomes of RQ in franchising relationship. Lastly, our paper will highlight the effect of relationship value in influencing franchisees' loyalty in franchise networks "What is an effect of relationship value towards loyalty?" Therefore, this paper will address the factors contributing to a successful long-term franchising relationship.

## **LITERATURE REVIEW AND CONCEPTUAL FRAMEWORK**

Social exchange theory (SET) has been used as the main pillar in developing this research framework. SET is used intensively in the marketing field to explain what Blau (1964) defines as "social exchange as here conceived is limited to actions that are contingent on rewarding reactions from others". Social Exchange Theory is used to explain the interaction between individuals or organizational members who are involved in any transactions with the expectation of a reward and avoidance of penalties or punishments (Emerson, 1976; Macaulay, 1963; Narasimhan, Nair, Griffith, Arlbjörn, & Bendoly, 2009). Based on SET, the researcher is developing research framework by identified two main constructs to strengthen franchise relationship namely relationship value and RQ.

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 (Ulaga, 2003). Relationship value has become more important since the transmission shift from transactional to relational marketing orientation (Walter, Mueller, & Helfert, 2000). Patterson and Spreng (1997) suggest that values have a strong and significant effect on satisfaction and repurchase intentions. Furthermore, relationship value or perceived value is identified as the most important measure of gaining competitive sustainability and is considered as to be an important predictor and key determinant of customer satisfaction and loyalty (Parasuraman & Grewal, 2000).

The RQ concept is embedded in the field of relational marketing (RM) (Crosby, Evans et al. 1990). Most papers related to RQ found in the marketing channels (e.g. Dorsh et al., 1998; Kumar et al., 1995) and sales literature (Crosby et al., 1990, Bejou et al., 1996) have measured

the RQ between manufacturers-sellers and salespersons-customers. Nevertheless, the lack of focus regarding RQ in franchising literature has motivated us to better understand RQ in franchisor-franchisee relationships in determining positive outcomes for the companies. Based on meta-analysis conducted by Ishak & Jantan, (2010), they identified three major dimensions of RQ namely; trust, commitment, and relationship satisfaction, that have been used frequently in business-to-business studies. In line with this Ishak and Jantan (2010) findings, the researcher will include trust, commitment and satisfaction as the main constructs in franchise relationship quality.

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* (Ganesan, 1994; Kumar, Scheer, & Steenkamp, 1995). 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 (Monroy & Alzola, 2005). Meyer and Allen (1991) conceptualize commitment at three levels, namely affective, continuance (calculative) and normative commitment. However, most research uses the two levels of organizational commitment, namely: affective commitment and calculative commitment (Gounaris, 2005; Mathieu & Zajac, 1990). Both affective and calculative commitments have a positive relation to the partner's loyalty intention to remain in the business relationship (De Ruyter, Moorman, & Lemmink, 2001). Numerous studies found that commitment is related positively to a higher performance level (Hausman, 2001), meanwhile other studies find that commitment correlates positively with relational benefits outcomes such as loyalty (Caceres & Paparoidamis, 2007).

Franchise satisfaction highlights the importance of mutual agreement between the franchisor and the franchisee pertaining to their contractual obligation, goal achievement and the franchisor's fairness among franchisees (Davies, Lassar, Manolis, Prince, & Winsor, 2011). The evaluation of franchisee's satisfaction is based on the franchisee's experience with the sum total of products and transactions during the life span of the franchising relationship. Morrison (1997) notes that satisfied franchisees are likely to be more profitable than dissatisfied franchisees. The franchisee's satisfaction towards his/her franchisor will positively affect the franchise performance and affect franchisee to stay loyalty in franchise business (Dickey, McKnight, & George, 2007). Furthermore, franchisees who are satisfied and profitable are likely to expand their business by opening new outlets and to promote prospective franchisees to join the franchise system (Dickey et al., 2007). On the basis of the preceding discussion, the following hypotheses can be developed:

H1: There is a positive relationship between RV and RQ.

H2: There is a positive relationship between RQ and loyalty

H3: There is a positive relationship between RV and loyalty

## **METHODOLOGY**

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 RQ, 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 (2006). The measurement of relationship quality (RQ) used three dimensions, namely trust, commitment and satisfaction. The RQ was conceptualized as a composite or multi-dimensional constructs consisting of different dimensions but related facets of a relationship (Palmatier, Dant, Grewal, & Evans, 2006). Trust was measured by six items, commitment was measured by seven items and satisfaction was measured by three items. All RQ items are adopted from various studies such as Ruiz-Molina, Gil-Saura, & Moliner-Velázquez (2010), Cater & Cater (2010), Gounaris (2005) and Rajaobelina and Bergeron (2009). Franchisee loyalty was measured by two items each for behavioral and attitudinal loyalty. Four items of franchisee loyalty were adapted from Gilliland and Bello (2002). 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 AND FINDINGS**

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 (Ringle, Wende, & Will, 2005). 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 (Graber, Czellar, & Denis, 2002).

In order to proceed with SEM-PLS, there are two stages for performing SEM which consist of a measurement model and structural model (Anderson & Gerbing, 1988; Hair, Ringle, & Sarstedt, 2011). 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 (Bagozzi & Yi, 1988; Gefen, Straub, & Boudreau, 2000; Nunnally & Bernstein, 1994). After all measurement of all constructs have adequate reliability and validity assessment, all the measurement items are kept for testing the structure model. The result of measurement structure is presented in Table 1. The composite reliability values for all the

constructs as tabulated in Table 1 are greater than 0.70. The results of composite reliability demonstrate that all constructs have adequate reliability assessment scores. In addition, the result for all measurement items loading are above the recommended value of 0.675, indicating that at least 50 percent of the variance in the observed variable is explained by the constructs. The AVE of all latent constructs ranges from 0.650 to 0.840, which exceeds the recommended level of 0.50 (Hair, Black, Babin, Anderson, & Tatham, 2006).

Table 1 Measurement model

Constructs	Items	Loading	CRa	AVEb
Loyalty	LY1	0.831	0.936	0.784
LY2		0.917		
LY3		0.881		
LY4		0.910		
RQ	RQ_CMT	0.926	0.940	0.840
RQ_SS		0.915		
RQ_TT		0.909		
RV	RV1	0.797	0.917	0.650
RV2		0.675		
RV3		0.806		
RV4		0.846		
RV5		0.844		
RV6		0.856		

a 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)}

b 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)}

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.

Table 2 Discriminant validity of constructs

Construct	Loyalty	RQ	RV
Loyalty	<b>0.885</b>		
RQ	0.752	<b>0.916</b>	
RV	0.684	0.785	<b>0.806</b>

Diagonals (in bold) represent the average variance extracted while the other entries represent the squared correlations

Next, the SmartPLS was used to run the hypotheses testing. 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 (Hammedi, Riel, & Sasovova, 2011). PLS uses re-sampling procedures known as nonparametric bootstrapping to evaluate the significance of the parameter estimates (Henseler, Ringle, & Sinkovics, 2009). In this study, the researcher uses 5000 resampling procedures for

bootstrapping as aligned with previous studies in the business-to-business context (Hair et al., 2011).

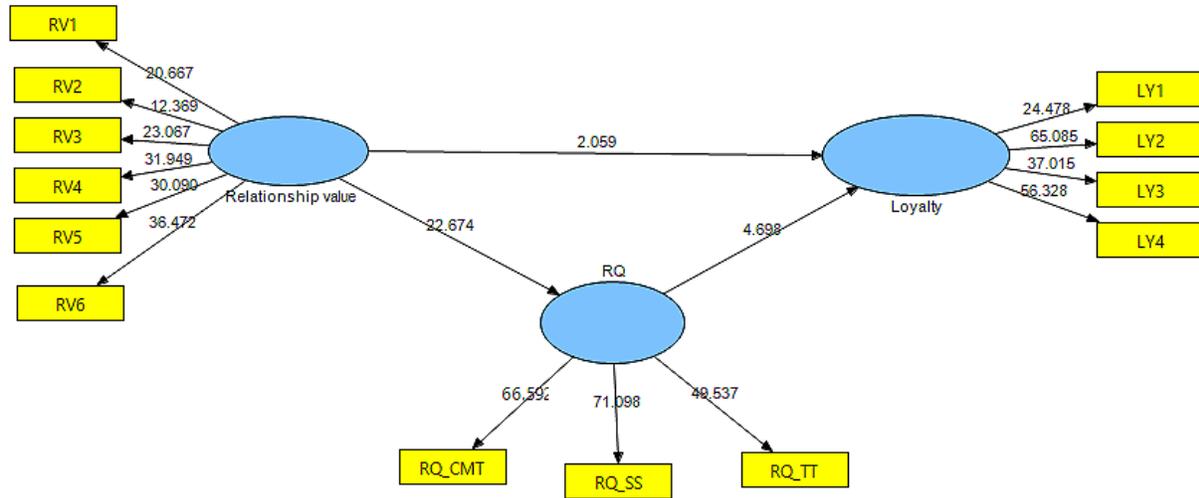


Figure 2 Results of the path analysis

Table 3 Path coefficient and hypotheses testing

Relationship	Coefficient (B)	T-value	Result
RV -> RQ	0.785	22.674	Supported
RQ -> Loyalty	0.561	4.698	Supported
RV -> Loyalty	0.244	2.059	Supported

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

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 supported at a minimum of  $p < .001$ . RV is positively related to RQ, whereas RQ is positively related to franchisee's loyalty. Furthermore, RV also positively related to loyalty. Therefore, all hypotheses in this study; H1, H2 and H3 are accepted.

## DISCUSSION AND CONCLUSION

Our study highlights the importance of relational value in influencing franchisee RQ. This study also shows that RQ is positively influencing in franchisee's loyalty to stay in franchise systems from a Malaysian perspective. Furthermore, three dimensions of RQ namely: trust, commitment and relationship satisfaction have become important indicators in franchise relationships quality similar to numerous studies in a business-to-business context (Bordonaba-Juste & Polo-Redondo, 2008a, Ivens, 2004). These three dimensions are important and inter-related in developing and strengthening the RQ in franchise relationship for a long term period. Similarly in franchise relationship which is characterized with high level of trust, commitment and satisfaction, franchisees will feel motivated to stay loyalty in ensuring their business is success. The positive relationship between relationship value and RQ reflects that the higher the

relationship value of the franchisee, the higher they tend to perceive themselves to be higher in trust, commitment and satisfaction. The link between relationship value and RQ indicates that franchisees really recognize all benefits received from the franchisor (such as training, services support, market analysis assistance, software support) over their investment in the franchise business. In conclusion, RQ in the context of the franchisee perspective consists of trust, commitment and satisfaction as important contributors in determining the franchisee's loyalty to stay in the franchise system. The development of RQ in a franchisor-franchisee relationship is critical in predicting important relational outcomes such as loyalty and performance. As it is inter-organizational dependency in the franchise system, one firm's success will depend on the other, achieving high RQ will result in the high performance of both parties for a long term business relationship.

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