Organizational Dynamics (2016) 45, 94—103

Available online at www.sciencedirect.com

ScienceDirect

journal homepage: www.elsevier.com/locate/orgdyn

Successfully managing chain-wide transformational change☆

Maryse J. Brand, Evelien P.M. Croonen, Dianne H.B. Welsh

> 'There is nothing more difficult to take in hand, more perilous to conduct, or more uncertain in its success, than to take the lead in the introduction of a new order of things.'
>
> — *Niccolo Machiavelli (1469—1527)*

THE NUMBER ONE ORGANIZATIONAL CHALLENGE

While decades ago innovative organizations were particularly known for their product innovations, nowadays this label is reserved for organizations that are able to adapt to changing landscapes by redesigning their business models. At the turn of the last century globalization was the driving force behind intensifying competition, and large international players were able to change the rules of the game. A decade later, the web-based economy — with powerful players such as Amazon, Alibaba, Netflix, and Google — is again redefining traditional sector boundaries and distribution methods and is forcing incumbents to either play by the new rules or quit. Playing by these new rules means being innovative by quickly adapting the business model and implementing the required changes successfully.

Managing change is the number one challenge identified by 48% of the businesses worldwide in a recent study. When organizations don't respond to developments in the environment their survival becomes threatened. The potential detrimental effect of a lack of organizational change is demonstrated by examples such as Howard Johnson's, Rexall Drug, Stuckey's, Blockbuster and Movie Gallery. In 2004, Blockbuster had over 9,000 company-owned and franchised units in the US with almost 60,000 employees. In 2010, it filed for bankruptcy due to not responding to competition from Netflix and Redbox. In 2013, it closed all its remaining company-owned stores and only the 50 franchised units remained open. Movie Gallery was the second largest retail movie rental store behind Blockbuster. It grew through the 2000s through acquisitions and takeovers, acquiring Hollywood Video. The company filed for bankruptcy in 2010 and closed its doors for the same reasons as Blockbuster.

Despite the importance of organizational change, 50—70% of changes fail during implementation. Implementing changes is especially challenging in chain organizations since they are a specific organizational form with unique problems. Chains typically become successful by replicating an attractive business format in a large number of units in different geographical locations. Well-known examples are McDonald's, Wal-Mart, Subway, Supercuts, CVS, Baskin Robbins, Home Depot, Holiday Inn, and 7-Eleven. Implementing chain-wide changes is a difficult challenge because units with varying characteristics and different geographical circumstances all have to adopt the same changes in a limited time period to maintain chain uniformity and economies of scale.

Introducing chain-wide changes is particularly difficult when units are owned by franchisees. Franchisees are independent business owners who make financial investments to adopt a franchisor's business format. Despite their investments in a more or less standardized format, franchisees typically have a certain desire for entrepreneurial autonomy and their goals may not always be aligned to headquarters' goals. When confronted with franchisor-initiated change, franchisees may thus adopt different responses and these responses largely affect the success of the change implementation process. Yet very little is known about how to implement changes in franchise chains and how to manage franchisee responses.

CHANGE IN FRANCHISED CHAINS

While franchising was introduced in the US around 1850 by Isaac Merritt Singer and Cyrus Hall McCormick, the

☆ This article was accepted by the former editors, Fred Luthans and John Slocum.

http://dx.doi.org/10.1016/j.orgdyn.2016.02.003

international launch of franchising began in the 1950s and 60s. Since then, franchising accounts for about 50 percent of retail trade in the US, 67 percent in Japan, and 44 percent of all retail trade worldwide. A recent survey among national franchise associations of 21 European countries points at over 12,000 franchised brands, about 750 of which are represented in a small country such as the Netherlands. International franchising is predicted to continue growing; 32% of the top US franchisors now operate units outside the US.

The popularity of franchising is understandable because it facilitates fast chain growth since franchisees invest their own resources in building and managing their units and are typically very committed to making their units successful. However, a main disadvantage for the franchisor is that franchising involves the complexity of managing a multitude of franchise relationships with legally independent franchisees that have their own goals. Examples of these complexities include Subway that suffered multiple lawsuits from their franchisees for putting units close together geographically, and Oil & Vinegar where franchisees contacted the Dutch media and filed lawsuits against the franchisor for mismanagement.

The franchisees' desire for autonomy and incongruent goals form a challenge for headquarters when trying to implement change. This challenge is even larger for transformational changes as compared to incremental changes. An example of an incremental change in a chain is the introduction of healthy alternatives such as apple slices and yogurt drinks in the McDonald's Happy Meal. Transformational changes require more franchisee investments and may result in more resistance, and thus require greater management focus. A recent example is the turnaround at McDonald's that was announced by CEO Steve Easterbrook in May 2015. This change requires costly equipment upgrades by franchisees (reportedly between $120,000 and $160,000) to adopt the 'Create Your Taste' strategy, resulting in several complaining franchisees covered by the media.

We look at the implementation of transformational changes to a chain's business format to better understand how to effectively manage this complex process. We conducted in-depth case studies in two large and competing Dutch drugstore franchise chains (ETOS and DA) that aimed to redesign their business formats during the increasing internationalization and competition in the early 2000s. We discuss the effectiveness of different change approaches and provide insights into how to promote desired and prevent undesired franchisee responses. The change process at ETOS was successful, whereas the one at DA was not. Comparing these change processes provides some valuable lessons on how to best manage changes in franchise chains. These lessons can be applied to other business contexts as well, especially chains with a centralized corporate organization and geographically dispersed units.

DRUGGISTS IN DISTRESS: TWO CONTRASTING CASES

The Dutch Drugstore Context

Historically, the product range of Dutch drugstores consists of four types of product groups: *health* (including nonprescription medicines), *beauty*, *personal grooming*, and *miscellaneous* product groups (including hair accessories). In the past decades, three drugstore chains have dominated the Dutch drugstore market: ETOS, DA, and Kruidvat.

The history of ETOS goes back to 1918 when personnel at Philips Electronics in Eindhoven started a cooperation with stores that could provide them with cheap day-to-day groceries. In 1973 the Dutch chain of Albert Heijn supermarkets took over all ETOS stores and turned them into drugstores. Both Albert Heijn and ETOS became subsidiaries of AHOLD, also founded in 1973. For many years, the ETOS chain consisted of only company-owned stores, but the number of ETOS franchisees grew steadily after the first franchisee started in 1988. ETOS gradually evolved from a discounting chain with only company-owned units to a high-quality chain with both company-owned (50%) and franchised units (50%) that all operated under a standardized business format.

The history of the DA chain goes back to World War II, when five Dutch druggists initiated a cooperative called 'DA'. They mainly wanted to establish a support network to share attractive purchasing deals. In the decades that followed, the number of DA members grew quickly, and DA turned into a 'cooperative franchise chain' with a central headquarters and a somewhat standardized business format. Even though headquarters had the formal rights to impose obligations on the DA franchisees, they did not do so for many years. DA franchisees highly valued their entrepreneurial autonomy and many of them wore white overcoats to indicate their professionalism. DA headquarters always aimed for only franchised units in the chain, no company-owned units. As is common in the Netherlands, both DA and ETOS had mainly single-unit franchisees; multi-unit franchisees usually only owned two or three units.

Compared to ETOS and DA, Kruidvat is a relatively young chain as it was started in 1975. It has always been a discounting drugstore chain with only company-owned units. The chain very quickly gained market share over time. In 1997, Kruidvat took over another discounting chain with only company-owned units (Trekpleister), and in 2002, both were bought by the China-based conglomerate AS Watson.

Distress at ETOS and DA

From the 1970s on, the Dutch drugstore industry faced radical changes in the business environment, which also affected DA and ETOS. First, a number of discounting drugstore chains — including Kruidvat — entered the market, confronting druggists with heavy price competition. Second, the entry of perfumery chains — such as Parfumerie Douglas in 1980 — challenged the traditionally strong position of Dutch druggists in perfumes and cosmetics. Third, new chains that integrated drugstore, perfumery, and pharmacy activities were emerging on the Dutch market, including the British Boots chain. Fourth, competition increased further as other nontraditional distribution channels — such as gasoline stations — began to offer health and personal care products. A final disturbing development was the start of a discussion at the Dutch government about opening up the market for nonprescription medicines.

In response to the above threats, both DA and ETOS headquarters initiated strategic changes from 2000 on. ETOS headquarters considered ETOS as being 'squeezed' between the discounter Kruidvat on the one side, and DA with its high