THE ROLE OF FRANCHISING IN MODERN DISTRIBUTION

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Abstract: In the paper Author recalls definition of the distribution, functions of the distribution and different types of agents. There are also presented strategies of the market internationalization and the role of franchising in the modern trade.

Keywords: distribution, franchising, market internationalization

1. The essence of distribution

Distribution can be defined as a process of market exchange. The aim of distribution as a marketing instrument of market influence is to provide buyers with products of appropriate quality in appropriate time, place and with the most comfortable forms and conditions of shopping at the lower available prices.
The structure of distribution includes:

1. Distribution channels (kind, structure, number, participants, institution supporting flow of market streams).
2. Physical distribution (service of orders, transport, maintaining and organizing warehouses and inventories).

2. Functions of distribution

In distribution process products overcome barriers: stock, quantity, time, ownership, spatial. All decisions and actions made by companies represent three groups of functions in the area of distribution:
Pre-transaction function, which realizes the following objectives:

- searching and reporting buy and sell offers,
- promotion of products and companies,
- negotiations of conditions of a contract,
- establishing business contacts,
- collecting and passing market information.

Pre-transaction function is particularly important because of coordination of supply and demand which takes place thanks to appropriate throughput of distribution channels. A practical implementation of above-mentioned functions is making a decision about a length, breadth and structure of distribution channel and connection between participants of the channel [1.].

Buy-sell realization function. The following items are associated with realization of purchase and sale transaction:
- carrying out orders,
- transport,
- maintaining inventory,
- using warehouses,
- trade processing,
- transporting products to intermediaries and final customers,
- transferring payments,
- acquiring risk,
- transforming production assortment into trade assortment.

From a broad perspective, this function is formulated by providing final customers with desired level of service with minimization of total cost of distribution. The function of buy-sell realization enables a physical flow of products from a producer to a customer, therefore it is identical to physical distribution of logistics of a distribution.
Post-transaction function includes:
- realization of rights of customers such as guarantees, warranties,
- various repairing, delivery and installation services,
- analysis of the level of customer satisfaction associated with purchased products,
- collecting data about potential customer requirements and wishes.

Analysis of the level of customer satisfaction associated with the purchased products, collecting information about expectations concerning forms and standards of service required by a customer and analysis of reasons of losing customers proves that the main goal of post-transaction function is to maintain relations and contact with customers. There are other equally important factors of this function such as: satisfying needs and customers' expectations and influencing the level of loyalty. Functions of distribution may cover also realization of product sale by producers themselves – direct distribution and ordering intermediary company sale functions – indirect distribution. A relatively important division of functions can be noticed between a producer and intermediary. Most often, producer takes care of realization associated with general establishment of principles of sales, that is price policy, conditions of deliveries, and supplying distribution channels – sales promotion, training, warehouses supply. On the other hand intermediaries are directed to realization of such important function as physical distribution. Physical distribution includes ordering, warehousing, realization of customer deliveries, completing of product assortment. Intermediaries take the risk associated with business activity through maintaining appropriate level of inventories and maintenance services. Both direct and indirect distribution goals can be summarized in the following points: targeting maximal amount of potential customers and transforming them into real purchasers, creation of consumer loyalty – and in consequence increase in sales, profits and market share [2.].

3. Types of intermediaries in a distribution channels

Intermediaries, on the basis of participation in the flow of ownership rights of product can be classified as follows:
1. intermediaries – buyers which takeover the right of ownership to products (wholesalers, retailers); in its own name and act as independent traders which buy products in order to resale them bearing all associated business risk,

2. intermediaries – agents which does not buy products but actively act in order to finalize buy-sell transactions (agents, brokers); this type of intermediary buys and sells products in the name of principal. They receive a fee for their services. An agent or a broker can represent a producer or seller [3.].

A producer, when choosing an intermediary should take into consideration the following parameters:

1. A kind of assortment sold by an intermediary.
2. The market volume, level of market penetration, density of distribution network.
3. Costs of distribution (conditions of payment, credits, discounts).
4. Partners' loyalty, forms of cooperation in the distribution channel.
5. Influence on partners' behaviour, including the level of prices, promotions or the quality of services [4.].

4. Wholesalers

Wholesale trade is organized in order to resale products for a further processing. Discrepancies between the area of production and consumption determine the wholesale structure. The most important determinants are summarized below:

1. Spatial distance between the production and consumption spheres.
2. Incompatibility between these two spheres with regard to the time of production and consumption of products.
3. Differences in amounts of produced products in relation to volume of products purchased by final buyers.
4. Different grouping of products: in the area of production according to raw material or technology, and in the area of retail trade according to clients needs [5.].

The goals of wholesalers activity are summarized below:

- purchase of larger, relatively homogenous lots of products,
- resale of products to retailers, other wholesalers or institutional buyers with profit,
- market research,
- searching and establishing relationships,
- negotiations of buy-sell conditions,
- transfer of the right of ownership,
- acquiring and storing products,
- transforming production assortment to trade assortment,
- adjusting products to needs of the final buyers (packing),
- crediting customers (providing financial assistance associated with a transaction),
- product insurance,
- product promotion [6.].

5. Types of wholesalers

Among wholesalers there can be three categories distinguished:

1. Wholesalers which buy products on its own cost and risk, can be divided to:
    a. wholesalers which realize the full range of services; such companies offer their customer a purchase and/or sale of products, storage, transport, financing of a transaction.,
    b. import and export wholesalers (apart from standard services they must provide customers with customs, transport and insurance services),

   c. wholesalers which supply retailers on the basis of commission sale; this kind of activity concerns fast moving consumer goods such as: cosmetics, magazines, over-the-counter medicines; supermarkets are main clients,
   d. wholesalers with limited range of services, which include:
      - cash & carry halls,
      - wholesalers realizing mail-order trade (on the basis of telephone orders, or mail orders); majority of clients are institutional customer.
2. Branches and sale offices of producers which are established for instance because of lack of appropriate wholesalers or in order to boost profits of producing company. This category of entities include:
   a. sale offices without warehouses which execute supplies directly from a producer to a buyer,
   b. sale branches which manage warehouses and operate much quickly than sale offices, but the costs of operations are higher.
3. Agency, which can be divided to:
   a. trade agents representing usually several noncompeting producers in a situation where managing own sale offices is unprofitable; trade agents receive a fee from sale but don't have any influence on distribution or a price of a product,
   b. brokers which are intermediaries in transactions between entities that are not connected with them apart from this single transaction; their role is to inform, negotiate and control orders.

Wholesalers on the consumer market can be classified as follows:

1. Traditional types of wholesaler which fulfill a very broad range of functions – they are called distributors. These type of companies are independent with regard to the form of ownership and management style. Distributors buy products and become their owners which is associated with business risk. This category of wholesalers includes:
   – general wholesalers (they offer various products: they provide constant delivery of products commonly available),
   – sector wholesalers (they offer products from one industry/sector),
   – specialized wholesalers (they sell a very limited and specialized assortment of products) or service a particular segment of customers (for instance gluten-free food).
2. Wholesalers with limited functions such as: commission sale, mobile procurement, cash & carry semi wholesalers [7.].
   Modern market decreases importance of wholesalers which nevertheless doesn't change their role associated with the function of creating value.
3. Organized market of wholesalers which enables concentration of trade and its location, including:
   – commodity exchanges, where participants meet and agree on prices on the basis of demand and supply; commodity exchanges are places where mass products are traded (coffee, sugar, skins),
   – bidding which are a quasi ranking of suppliers; among many offers an bidding committee chooses the best offer for customer,
   – auctions which are a type of exchange and are organized in order to sell unusual products using public auctions,

- fairs and exhibitions which are a form of promotion and establishing business contacts rather than a buy and sell transactions place; during fairs or exhibitions companies may sign contracts which are realized after the meeting.

6. Market internationalization

In relation to large chains of supermarkets four strategies of internationalization in entering the market can be distinguished:

1. Own investments (purchase of land, construction of buildings from foundations); this kind of strategy is used in Poland by Western chains of retailers, but they currently to a larger extent use services of logistics operators.
2. Acquisition of local chains of supermarkets.
3. Joint ventures with local partners.
4. Franchising [7.].

Modern global markets are dominated by large market chains which changes the position of a wholesaler in a distribution process. The role of franchising as a distribution system gains more importance. Economic internationalization is among others associated with increase of relevance of fast moving consumer goods (FMCG). Current market is dominated by an activity of large chains of supermarkets which determine new paradigms of organization and management in distribution. Development of modern distribution has caused a decrease of the role of traditional trade.

7. Franchising

(…)"Franchising can be described as a distribution system, in which on of parties (a franchisor) gives to the other party (a franchisee) a right to distribute products, provide services and conduct business activity in accordance with determined marketing system. Franchisor provides franchisee with a knowledge, experience trademark, company image and initial and current support. In return, franchisee pays a fee for franchisor" [8.]. Thanks to a franchising agreement one of business partners is privileged. He has an exclusive right to sell particular products or services on a strictly defined market, or a right to product goods using know-how and technology of a franchisor. "Franchising agreement usually concerns conditions of cooperation, which are associated with transfers between agreement parties (mainly in association with cash transfers from franchisees to franchisors and technology or know-how transfer from franchisor to franchisees). The agreement specifies also restrictions concerning both franchisor and franchisees" [9.].

Advantages of franchising agreement:

- a possibility of using reputation, a brand of franchisor and proven in practice concept of business model;
- lower risk associated with establishing business entrepreneurship;
- specialized knowledge or experience in the are where the business operates is not necessary;
- franchisee receives the exclusive right to sell products or offer services in the particular area;
- universal support from a franchisor is available;
- lower capital expenditures connected with opening franchise unit;
- benefits from national marketing actions;
- benefits from a large scale of operations of franchise network;
- a possibility of using research and development programs of franchisor.

Drawbacks of franchising:
- royalty fee;
- selling only imposed products and offering indicated services;
- limitations of franchisees with regard to sale of a company;
- wrong policy of a franchisor;
- a good image of franchising network and particular brand may lose reputation because of event or reasons not attributable to franchisee.

Franchising agreement is a legal document, where transaction between franchisor and franchisee is described in a comprehensive way. This is not represented by the level of details but on a just and precise description of a model of cooperation between parties, with consideration of control mechanisms, which enables franchisor to maintain cohesion of the system.
There are various models of franchising systems proposed by Western franchisors:
1. The amount of initial investment of franchisor; in Poland market chains inform about various amounts.
2. The amount of initial fee; in Poland this is not a barrier for domestic franchisees (there aren't any initial license fees).
3. The period of franchising agreement; it may be agreed on 5, 10 years or undefined time.
4. Possibility of organizing and running several sales points by a franchisee.
5. Franchisor may limit exclusiveness of franchisee to a given area.
6. Marketing activity can be conducted by franchisee on the local level; if a market chain covers the whole country, franchisor organizes marketing on the national level.
7. Network (e.g. market chain) usually enables franchisees to choose preferred form of business activity.

Book running; majority of networks accepts choices of franchisee [7.].

8. The scope of franchising

There are a multiple types of business organized in a form of franchising, among others, recreation clubs, tourist offices, tourist centres, motels, restaurants, fast food bars, sport shops, camping, and also points which deduct taxes from their income, car rental companies, DVD and video rental shop, branches of real estate agencies, beauty centres, hairdressers and professional offices, and even oil refinery. Franchising is used in selling cars, trucks and agricultural equipment. Usually dealer has a guarantee of territorial exclusiveness, consultancy and training of new employees. Franchising develops very fast. Retailers prefer to invest money under a brand of well known intermediary of producer. Risk associated with franchising is connected with incompetent and inadequate use of verified procedures and organization of product sale, and a passive attitude of retailer towards volatile and changing situation on the market.

9. Franchising in Poland

Franchising develops in Poland mainly in the area of:
- trade – clothes shops are most popular in Poland (e.g. Reserved, Cropp Town, House),
- services – gastronomic points.

Among agency systems in:

- grocery and chemical shops (e.g. Zabka or press points of Kolporter),
- services – financial intermediaries (e.g. partnership branches of Eurobank, ING or Expander).

Polish franchising abroad is present mainly in neighbouring countries; almost 25% of franchising brands starts its development in Czech Republic. 40 Polish franchisors successfully sell their licenses on business abroad, and next 38 plans foreign expansion. Currently, there are thirteen banks which offer licenses on business abroad using their logo or brand, for instance Getin Bank, ING, Multibank, Bank PKO SA, Bank PKO BP. Banking networks more often cooperate with partners who open more than one branch using the same license – multi-franchising. At the end of June 2008 Polish market consisted of approximately 3303 licensed branches (including PKO BO agencies). In the first half of 2008 banks have established more than 250 franchising branches. The largest dynamics in increase of partnership branches in this period have been noted by BPH (89) Getin Bank (68) and GE Money Bank (46). More than twenty openings were realized also by Dominet Bank, MiniBank oraz Eurobank.

10. Conclusion

In the area of retail trade, there are multiple tendencies visible that indicate a formulation of new model of distribution. Retailers are becoming consolidated, traditional retailers decrease in number and importance, and new types emerge and gain greater relevance – discount stores, supermarkets, hypermarkets. There are sale strategies created by producers and distributors, which are based on direct sale to large retailers and wholesalers. Nowadays, large chains dominate in distribution channels. Franchising as a form of distribution organization becomes more and more popular.

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