CORPORATE CHAINS VERSUS CONTRACTUAL CHAINS:

EXAMINING COMPETITION AND STORE DEVELOPMENT IN THE CASE OF

THE AUTO PARTS RETAILING INDUSTRY

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ABSTRACT

Having an optimal number of retail outlets in a market is important to understanding the effectiveness franchised systems versus corporate systems. In traditional franchise systems, where the franchisor has shared incentives to increase sales with a franchised-retailer, overstoring a market is avoided in that the wholesaler-franchisor shares in the cost of goods to the retailer franchisee, keeping the number of stores near optimal to maximize gross margins of both parties. This is in contrast to business format franchising, where the franchisor’s sales to the franchisee are not a significant proportion of franchisor revenues when compared to royalties based on net sales.

Attention is given here to the costs of a franchisee retailer’s inventory investment, similar to a “lump-sum” investment in franchise systems. In wholesale franchisor systems, there are short-term incentives to overstore a market to increase initial sales to franchisees of inventory, and there may be cost advantages in inventory replenishment. Franchise systems, however, compete with wholly corporate systems, and there are no apparent reasons to overstore in systems with single, unified ownership. Evidence showing that the suppliers to the corporate systems are providing increasingly favorable financing of inventory, leading to a possible explanation as to why they too might have more stores than optimal, with strategies more comparable to franchise chains. This hypothesis is examined across competing chains in auto parts, and the response to coverage and saturation, stores per person and sales per store, respectively. The shares of the eight top auto parts chains in 448 U.S. markets are analyzed, and the results show significant differences in strategy among the company-owned chains and wholesaler sponsored, or contractual chains.

KEYWORDS: coverage, markups, auto parts, inventory, corporate chains