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Jakob Utgård

Organizational form, local market structure and corporate social performance in retail

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Market structure, chain membership and food hygiene in retail

Paper 3:
Retail chains' corporate social responsibility signaling

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by

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Abstract

I study how organizational form and local market structure influence retail firms' corporate social performance (CSP). The theoretical model is based on agency theory, which in its origin focuses on the dyad between the principal and the agent. I extend this perspective and examine how characteristics of the environment outside the dyad influence the outcomes. Retail stores vary in their organizational form and thereby in their incentives to maximize profits. I hypothesize that the different incentives, together with differences in monitoring costs and principal demand influence CSP. Further, developments in agency theory have suggested that the local market structure can influence the effects of the chain-store contracts. Competition can give corporate stores stronger incentives to maximize profits, and reputation effects can increase the profitability of CSP. The main contribution of this dissertation is testing these predictions empirically with data on the CSP of retail stores and chains. The dissertation consists of an introduction, three independent empirical articles, and a conclusion.

In the first article (“Franchising, local market characteristics and alcohol sales to minors in retail”) I study how the influence of organizational form (franchised vs corporate store) on CSP depends on competition, market size and public monitoring and sanctions. As the measure of CSP I use the results of alcohol purchase attempts done by underage teens in retail stores. Control variables are collected from other sources. As hypothesized I find that franchised stores are more likely to sell alcohol to minors, and that they are more sensitive to the risk of sanctions. However, I find no relationship between competition and performance, and corporate stores and not franchised stores improve their performance in small markets.

The second article (“Market structure, chain membership and food hygiene in retail”) studies how chain membership and competition influence food hygiene in supermarkets. In Denmark, the “Smiley scheme” makes the results of hygiene inspections by food authorities public. I hypothesize a U-shaped relationship where low and high levels of competition give better quality, since stores with little competition are located in small markets with strong reputation effects. I further hypothesize that chain stores are less sensitive to competition, since chains standardize quality. I get robust support for the U-shaped relationship between competition and quality, but limited support for the lower sensitivity of chain stores to competition.

In the third article (“Retail chains’ corporate social responsibility signaling”) I study how the retail chain's organizational form influences its CSP signaling. I hypothesize that vertically integrated chains are more likely to signal CSP since they have less problems getting their stores to commit to common investments in CSP than other chains. I also include other hypotheses testing signaling theory. The data comes from a content analysis of the web pages of 208 retail chains in the Norwegian market, combined with information from other sources. As hypothesized, I find that franchise chains are significantly less likely and plural and voluntary chains marginally less likely to signal CSP than integrated chains. Two of the other three hypotheses testing signaling theory are supported.

In total, the findings give partial support to agency theory. For the direct effects of organizational form the hypotheses are supported. Franchised stores have lower social performance when monitoring costs are high but there are smaller differences between independent and chain stores when monitoring costs are lower. The chain-store contract also has consequences for CSP at the chain level. For the moderating effects of the local market structure, agency theory is not supported.

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Oslo, October 2014

1 Introduction

To build and maintain their reputation and competitive position and achieve economies of scale, retail chains standardize many parts of their operations across their store network (Mathewson and Winter 1985; Ingram and Baum 1997). Prices and products are relatively similar, quality and service levels comparable, and marketing campaigns and opening hours coordinated. At the same time stores and store managers have to be encouraged to run as efficiently as possible by cutting costs and increasing sales and profits, and given sufficient freedom to adjust to different local market conditions (Sorenson and Sørensen 2001). The chain has to find the balance between incentives and standardization; too strong economic incentives can lead the store manager to abandon the chain standards and reduce quality below what is acceptable to increase his or her personal financial gains, too weak incentives can lead the store manager to be indifferent and do a poor job.

A theory much used to study such problems of retail organization is agency theory. Agency theory uses the metaphor of the contract to study relationships where one party (the principal) delegates work to another party (the agent) (Eisenhardt 1989; Shapiro 2005). For retail chains, an important question is whether to use franchised stores, where the store is owned and operated by an independent party with a contract specifying the terms, or corporate stores, where the chain employs the store manager. This choice of organizational form can have consequences for different types of store performance, the franchisee has strong financial incentives to maximize sales and minimize costs, but may go too far and reduce quality below an acceptable level for the chain (Kidwell and Nygaard 2011; Michael 2000). A considerable literature has studied the free riding problem in franchising (e.g. Kidwell, Nygaard, and Silkoset 2007; Michael 2000; Rokkan and Buvik 2003). Free riding occurs when a store gets the benefits from belonging to the chain but does not take its part of the costs (Kidwell, Nygaard, and Silkoset 2007, 525). Since franchisees keep their own profits they have incentives to reduce quality if it benefits them, also when this comes at the expense of the other members of the chain who suffers from a worse reputation. The reality of this problem has been confirmed empirically. Franchised units have worse hygiene than corporate units belonging to the same chain (Jin and Leslie 2009), are more likely to break laws to gain extra profits (Pierce and Toffel 2013), charge more for the same products (Ater and Rigbi 2013; Wilson 2012a), and are more likely to pay their employees less than they are obliged to by law (Ji and Weil 2009).

What is notable about these empirical studies is that they do not only show how free riding affects the chain's reputation, which can be damaged should information about the poor performance become public, but also how the free riding negatively affects third parties, such as customers, employees or society in general. The strong financial incentives of franchising make stores maximize their profits, sometimes at the expense of others. Treatment of third parties is part of a firm's corporate social performance (CSP). CSP is briefly defined as "corporate pro-social behavior" (Luo and Bhattacharya 2009, 201), or more extensively as a "business organization's configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationships" (Wood 1991, 673). In essence, CSP measures whether a firm behaves acceptably by legal and ethical standards towards others, by following laws and regulations and respecting the integrity and well-being of those affected by the firm's operations. The first purpose of this dissertation is to examine the effect of the chain-store contract/organizational form on CSP. Do franchised stores have lower CSP than corporate stores, like the findings in the literature on free riding suggest? If so, do independent stores, with stronger financial incentives and no chain to control their behavior, have yet lower levels of CSP?

In agency theory the unit of analysis is the contract between the principal and the agent. However, all dyadic relationships are embedded in a wider set of social and economic institutions with the potential to influence the behavior of the parties, including how they write and respond to the contract (Granovetter 1985). In marketing, the importance of the environment surrounding marketing channels has long been recognized (Arndt 1981; Achrol, Reve, and Stern 1983). Developments in agency theory have also acknowledged that characteristics of the markets outside the dyad, such as competition and reputation effects, can influence the outcomes of different types of contracts (Hart 1983; Shapiro 1982). Competition can make managers of corporate stores more efficient as they have to work harder to keep up with competitors (Tirole 1988). Reputation effects can reduce the profitability of free riding for franchised stores, as the true quality of the firm becomes known to customers (Jin and Leslie 2009). The second main purpose of this study is to examine how characteristics of the local market such as competition and market size interact with the chain-store contract to shape store social performance. Previous studies have examined the consequences of the local market structure for the choice of organizational form (Dahlstrom et al. 2009; Nygaard and Myrtveit 2000). In this dissertation I go one step further and examine actual performance outcomes when different types of contracts meet different types of market structures.

The dissertation is structured in the following way: This introductory chapter presents the theoretical framework and describes the main research model. Three independent empirical articles follow. Finally, the concluding chapter sums up the findings and contributions.

1.1 Theoretical framework: Agency theory in retail

Agency theory uses the metaphor of the contract to model relationships where one party (the principal) delegates work to another (the agent) (Eisenhardt 1989). The principal-agent problem generally deals with "motivating one person or organization to act on behalf of another" (Milgrom and Roberts 1992). The principal and the agent typically have different interests, the principal wants maximum effort for minimum pay and the agent wants maximum pay for minimum effort. The principal has to design the optimal contract for the agent, taking into account the costs of monitoring the agent, since the agent always will have more information about his own effort and performance. The principal has two general options for this, either a behavior-based or an outcome-based contract. Eisenhardt (1989, 58) sums up the theory in the following way: "the focus of the theory is on determining the most efficient contract governing the principal-agent relationship (…). Specifically, the question becomes, is a behavior-oriented contract (e.g., salaries, hierarchical governance) more efficient than an outcome-oriented contract (e.g., commissions, stock options, transfer of property rights, market governance)?". The outcome-based contract aligns the interests of the parties to a larger degree. However, since the agent is more risk-averse than the principal and since the outcomes are partly decided by factors outside his control, the agent may be reluctant or demand a high premium to accept this (Bergen, Dutta, and Walker Jr. 1992). Agency theory has been used to study a wide range of phenomena in economics, management, marketing, law and sociology (Shapiro 2005). In marketing, agency relationships are abundant since exchange between two parties is the essence (Bergen, Dutta, and Walker Jr. 1992). Agency theory has therefore been applied on issues such as how to organize interorganizational relationships (Mishra, Heide, and Cort 1998) and how to compensate salespeople (Eisenhardt 1988; Anderson and Oliver 1987).

In retail, empirical studies have used agency theory to study chain organization (Dant, Grünhagen, and Windsperger 2011; Brickley and Dark 1987; Combs, Michael, and Castrogiovanni 2004). The central problem has been whether retail chains are better off using franchised or corporate stores. In retail franchising, the chain (franchisor) sells the rights to use the brand name and business systems to the store owner (franchisee). The franchisee normally has to provide an initial investment in the store, and pays royalties, often as a percentage of the sales, to the franchisor. The franchisee has the right to the profit after the costs are paid. In corporate stores, the store manager is an employee and the chain has the right to any profits. Franchisees have strong financial incentives to maximize their profits, which aligns their interests with those of the chain, who also are interested in increased sales and reduced costs. However, the problem for the retail chain with using franchising is the potential free riding by the stores. Free riding occurs "when an individual obtains indivisible benefits from being a member of a group but does not bear a proportional share of the costs" (Kidwell, Nygaard, and Silkoset 2007, 525). Since franchisees maximize their own profits, they have incentives to reduce investments in activities that they only partly get the benefits from, such as activities relating to the reputation of the chain as a whole (Lafontaine 1999). Such activities can be product and service quality or common marketing activities. To make sure that stores adhere to quality standards, chains monitor the performance of their stores, but, monitoring is costly, and even with high investments in monitoring it is impossible to measure all dimensions of performance perfectly. Research has therefore focused on how the monitoring costs influence the choice between franchised and corporate units. Where monitoring costs are high, franchised stores should be favored, and where monitoring costs are low, corporate stores should be more efficient (Combs, Michael, and Castrogiovanni 2009).

Agency theory has generally been supported empirically in the retail context (Combs, Michael, and Castrogiovanni 2004; Combs et al. 2011). For instance, empirical studies have found support for the influence of monitoring costs on choice of organizational form (Combs and Ketchen 2003). Longer distance from the headquarters and larger unit size, both variables that make monitoring more costly, increases the likelihood of franchising (Brickley and Dark 1987; Alon 2001). The danger of free riding has been used as an explanation for why franchised chains invest less in advertising than integrated chains (Michael 1999), and for why the percentage of franchised units in hotels and restaurant chains is negatively related to quality as perceived by the customer (Michael 2000). Recent studies have also found support for the free riding hypothesis at the store level. For instance, franchised restaurants have been found to have worse food hygiene than corporate stores belonging to the same chain (Jin and Leslie 2009), and franchised restaurants have larger amounts of back-wages (wages owed to their employees but not paid) than corporate restaurants in the same chains (Ji and Weil 2009).

While much of the research using agency theory in retail has focused on explaining the choice between franchising and corporate units, the theory has also been applied on other types of organizations in retail. Agency theory may be used to explain the existence of retail chains overall (Dahlstrom et al. 2009). Chain stores have to follow specific standards, and give up some freedom for the benefits that follow common standards, such as reputation and economies of scale (Ingram and Baum 1997; Kosová and Lafontaine 2012). If it is too difficult to maintain a common standard due to the risk of free riding, independent units will be more efficient. Table 1 gives a summary of the different organizational forms in retail, highlighting the differences in incentives at the store level and chain management control over the store.

Table 1: Contracts in retail

	Independent store	**Franchised store**	**Corporate store**
General description	Independently owned and operated store	Franchisee operates store according to contract with chain (franchisor)	Retail chain owns and operates store through store manager
Investments and incentives	Owner makes investments and has the right to profits	Franchisor and franchisee both makes investments. Franchisee has right to profits, franchisor normally gets % of sales as royalty	Retail chain makes investments and has the right to the profits
Chain control over store	None	High – chain controls products, prices, brand concept. Franchisee mainly in charge of personnel	Highest – chain controls everything

Partly adapted from Dahlstrom et al. (2009, 843)

1.1.1 The influence of the local market structure in agency theory

In its origin agency theory mainly deals with the contract between the principal and the agent. However, all dyadic relationships are embedded in a wider set of social and economic institutions with the potential to influence the behavior of the parties, including how they write and respond to the contract (Granovetter 1985) In marketing, the importance of the economic and institutional environment surrounding marketing channels has long been recognized (Arndt 1981; Achrol, Reve, and Stern 1983; Grewal and Dharwadkar 2002; Anderson, Håkansson, and Johanson 1994). The political economy framework in marketing (Stern and Reve 1980; Arndt 1983) sees marketing channels as political economies consisting of the distribution channel and the channel environment, where the environment influences the outcomes in the channel. Related research in marketing has used the basic insight that contracts are influenced by the surrounding channel environment, and among other things studied how incentives and governance mechanisms in one relationship influence other relationships (Wathne and Heide 2004; Kumar, Heide, and Wathne 2011) and how dependence (the lack of outside alternatives) between the exchange partners influence their relationship (Gundlach and Cadotte 1994; Kumar, Scheer, and Steenkamp 1995; Gulati and Sytch 2007).

The potential influence of the local market has also been recognized in agency theory, and some studies have examined how competition and reputation influence the outcome of contracts. Agency theorists have suggested that the competitive pressures of the market may work as an incentive scheme in itself (Hart 1983). If competition is tough, managers have the incentives to improve the performance of their units to stay in business, especially since they may be competing with other firms where the owner is also the manager and who therefore do not have the same principal-agent problem. The slack necessary for the managers to shirk their responsibilities is simply not available in highly competitive markets (Tirole 1988). Even store managers will be concerned about tough competition, as their job may be in danger if they perform poorly. In the case of retail, this means that independent stores, franchised stores and corporate stores would compete in the same market, and the competition from independent and franchised stores would constrain the managers of the corporate stores (Nygaard and Myrtveit 2000). Based on this theory, retail chains should use corporate stores to a higher degree in markets with tough competition. Empirical tests of this prediction have however not found support for this (Nygaard and Myrtveit 2000; Dahlstrom et al. 2009).

Agency theory has also recognized the role of reputation as a mechanism to ensure good quality (Klein and Leffler 1981; Shapiro 1982; Jin and Leslie 2009). Consumers and others can use the reputation of a firm or a product as a signal of quality, even if quality is directly unobservable to them. Free riding will then be less profitable for franchised stores, since they may lose customers. Previous research in franchising has focused on the role of reputation in the choice of organizational form. Since firm reputation can reduce the problem of free riding, franchising should be relatively more efficient in locations with strong reputation mechanisms and vertical integration more efficient in locations with weak reputation mechanisms. Empirical support is mixed. Brickley and Dark (1987) found that franchised units were more common in sectors with more repeat customers, and also that monitoring costs were lower in these sectors. However, when examining the organizational form of units close to highway, where there presumably are less repeat customers, they found significantly more franchised units, contrary to expectations. Kidwell et al. (2007) also found less free riding among franchisees located close to highways. On the other hand, Nygaard and Myrtveit (2000) found more company owned and operated dealers close to highways.

In total, while the potential influence of competition and reputation has been recognized in agency theory, empirical research in retail has given mixed results. Further, the studies have mainly examined the choice of organizational form and not the performance outcomes of such choices.

1.2 Corporate social performance

The dependent variable in this dissertation is corporate social performance (CSP). CSP is a concept much used and studied in the fields of management and strategy (Aguinis and Glavas 2012; Wood 2010) and has been defined as “corporate prosocial behavior” (Luo and Bhattacharya 2009, 201) or more extensively as a “business organization's configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationships” (Wood 1991, 693). CSP is closely related to a range of other concepts such as stakeholder theory, business ethics and corporate misbehavior, but in particular corporate social responsibility (CSR). CSR has been defined as “context-specific organizational actions and policies that take into account stakeholders' expectations and the triple bottom line of economic, social, and environmental performance” (Aguinis and Glavas 2012), or in the perspective of economics “the private provision of public goods” (Bagnoli and Watts 2003). The main difference between CSR and CSP is the added emphasis on actual performance outcomes in CSP. In one sense, CSP is the result of attempting to measure the CSR of a company (Crane and Matten 2010).

While CSP can be seen as part of firm or product quality, it emphasizes the total social impact of the firm's operations, including the consequences for third parties. CSP cover the treatment of the groups affected by the firm's operations, such as employees (a firm with high CSP for instance pays fair wages and secures a safe working environment), customers (a firm with high CSP for instance provides safe products of good quality and advertise honestly), suppliers (a firm with high CSP for instance writes fair contracts and do not behave opportunistically) and civil society (a firm with high CSP for instance pay fair taxes and support good causes). Some make a distinction between environmental and social performance, but others include environmental performance as a dimension of CSP, since all groups in society depend on the environment (Waddock and Graves 1997; Phillips and Reichart 2000).

CSP is a broad theoretical concept measured in many ways (Wood 2010). Some studies use indices of CSP (Siegel and Vitaliano 2007; Brammer and Millington 2008; Barnett and Salomon 2012). These indices are typically constructed by consultancies to investment firms, and include measures on involvement in activities that are seen as unethical (such as weapons production, alcohol, or nuclear power) as well as indicators on issues such as community relations, corporate governance, diversity, human rights and the environment (Wood 2010). One disadvantage with the indices is that they typically only exist for large, public firms. Other studies have used communication about social and environmental issues in annual reports, on web pages or through other channels as the measures of CSP (Fifka 2011), based on the assumption that firms with better performance are more likely to communicate about it. Since CSP deals with the impact of firms' on various stakeholders (groups that are affected by the firm's operations), it is also possible to measure this impact by asking the stakeholders directly. Customer satisfaction surveys, for instance, are measures of how satisfied one particular stakeholder is with an important part of the firm's activities (Wood 2010; Anderson, Fornell, and Lehmann 1994). Finally, CSP is also measured using different types of objective data such as the level of toxic emissions (Khanna and Damon 1999), number of announced product recalls (Chen, Ganesan, and Liu 2009) contributions to charity (Campbell and Slack 2006) or regulatory violations or crimes (Pfarrer et al. 2008).

A long-standing debate is whether high levels of CSP are a result of altruistic actions or a firm's strategic efforts to maximize profits (Siegel and Vitaliano 2007). The altruistic perspective suggests that owners or managers willingly sacrifice profits to benefit groups in society. Owners can based on their own preferences decide to provide better CSP than what will maximize profits, for instance by paying employees more than the market price or by not engaging in certain types of legal activities due to their own ethical preferences. Alternatively, the altruistic actions can be done by managers, who take advantage of the information asymmetries between themselves and their owners (the agency problem) and use firm resources for good causes instead of maximizing profits for the owners (Friedman 1970). The competing, strategic perspective of CSP suggests that firms use good CSP to improve their relationship with groups that the firm depends on, such as customers, employees, local communities, NGOs, media and regulators, thereby maximizing their profits (Campbell 2007; Aguinis and Glavas 2012). In the strategic perspective, good CSP can be used to improve the reputation and attractiveness of the firm and its products. Some empirical studies support this perspective. Firms with good CSP have higher customer satisfaction and are therefore more valuable (Luo and Bhattacharya 2006). Customers also are more forgiving with firms that have good CSP if an accident or negative event happens (Klein and Dawar 2004). In industrial markets, firms with good CSP have better relations with their customers or suppliers (Homburg, Stierl, and Bornemann 2013). Firms with good CSP are more attractive employers (Turban and Greening 1997; Jones, Willness, and Madey 2013), and employees are more committed and satisfied when they work for an employer with high CSP (Kim et al. 2010; Brammer, Millington, and Rayton 2007; Valentine and Fleischman 2008).

If firms use CSP as a strategic tool, firms with high CSP should be more profitable. The relationship between CSP and firm financial performance is much studied and contested (Griffin and Mahon 1997), but the latest evidence from meta-studies and reviews suggests a weak, positive relationship. Summarizing 52 previous quantitative studies, Orlitzky et al (2003) find a positive relationship for social and environmental performance on financial performance. In a review of 251 studies, Margolis et al (2009) also find a positive although weak relationship. Some recent studies have found a positive, U-shaped relationship, where low CSP gives better financial performance than moderate CSP and high CSP gives the best financial performance (Brammer and Millington 2008; Barnett and Salomon 2012). Recent studies with a research design more suitable to uncover a causal relationship have also found a positive relationship. Based on a regression discontinuity design, Flammer (Forthcoming) studies the adoption of CSR-related shareholder resolutions narrowly adopted (versus narrowly rejected), and finds that adopted CSR resolutions improves financial performance.

Another way of testing the strategic theory of CSP is to examine the relationship between competition and CSP (Fernández-Kranz and Santaló 2010). If CSP is a strategic tool to differentiate from competitors in the aim of attracting customers, employees or investors, higher levels of competition should give better CSP. The altruistic theory predicts the opposite, since tough competition gives less resources to devote to good causes. Fernández-Kranz and Santaló (2010) find robust evidence of a positive relationship between competition and CSP. They find market concentration negatively related to CSP, that increased competition due to higher import penetration improves CSP, and that firms in more competitive industries have better environmental performance. Other studies of competition and CSP find the same (Hawn and Kang 2013; Declerck and M'Zali 2014), including Flammer (Forthcoming), who finds that reductions in tariff rates which exposes domestic producers to more competition from abroad improve CSP for companies in the affected industries.

1.2.1 Agency theory and CSP

Agency theory, like the strategic view of CSP, suggests that firms will produce the level of CSP that maximizes their profits (Connelly, Ketchen, and Slater 2010). In a simple agency-theoretical model of CSP, groups interested in good CSP (the principals) contract the firm (the agent) to provide good CSP. The principals can be several groups, but owners, customers, employees and regulators may be particularly important, since these have direct ways of influencing the firm by giving or withdrawing financial support. Owners have the possibility of demanding good CSP directly from their firms. Even individual investors in anonymous public stock markets can reward firms based on CSP by investing only in firms that satisfy certain criteria for good CSP, or avoid investing in particularly poor performers. Similarly, customers can select firms and products that satisfy their personal preferences and employees can choose to work for firms with high levels of CSP, essentially making the cost of labor cheaper for such firms. Public authorities can draft laws and regulations, and use a variety of instruments to make firms follow them, including licensing systems, inspections and monitoring, and sanctions. Firms and in certain cases the managers and employees responsible who do not follow rules are faced with fines or other types of financial or criminal punishments. Such an "expanded" agency model goes beyond the typical owner-manager and manager-employee relationships often studied as principal-agent relationships. However, it is clear that all relationships where one party acts on behalf of another are agency relationships (Shapiro 2005), and that agency theory also applies to social and informal contracts and not only written, formal contracts (Bergen, Dutta, and Walker Jr. 1992).

Agency theory predicts that the firm (as the agent) will produce good CSP only when the principals demand it. For dimensions of CSP that are not demanded firms have no financial incentives to provide high levels of performance. The different principals may prioritize CSP that affect them directly. Customers' willingness to pay for environmental performance is for instance often found to be limited (Ambec and Lanoie 2008; Steg and Vlek 2009). Illustrating the importance of principal demand is the case of “unethical demand” (Pierce and Snyder 2013) where good CSP is the opposite of the interest of the customer. In vehicles emission testing, a private garage is responsible for testing whether a car has an acceptable emissions level. The customer wants the car to pass the inspection, but society wants acceptable emission levels. Unsurprisingly, a percentage of cars that pollute too much pass the test, since the garage and the customers share this interest (Bennett et al. 2013).

Another prediction following agency theory is the influence of monitoring costs on performance. One of the key dimensions in agency theory is information asymmetry. Typically, the agent has more information than the principal about his own performance or effort, and the principal has to design the optimal contract in this situation (Husted 2007; Banerjee 2002). The theoretical positive relationship between CSP and financial performance rests on relevant groups rewarding good performance by selecting or rewarding good performers over bad performers (Brammer and Millington 2008). The empirical studies of the CSP-financial performance relationship have mainly been based on easily observable measures of CSP, such as information disclosed by the firm itself or ratings by stakeholders. Since judgments of CSP can only be based on available information, the ratings may be biased. For dimensions of CSP where the information asymmetry is high and where outsiders have difficulties with ensuring performance, the relationship may not be positive. Many dimensions of social performance have very high monitoring costs for outsiders, including credence attributes (Darby and Karni 1973). Credence goods are products or services where an expert knows more about the quality than the consumer himself or herself, even after the consumer has bought and used the product (Dulleck and Kerschbamer 2006). It is for instance difficult to know whether a product has been produced with acceptable conditions for the workers along the supply chain, or with acceptable levels of pollution. Some dimensions of social performance, for instance animal welfare or fair trade, have “Potemkin attributes”, where the quality cannot be assessed at the end product by for instance government agencies or consumer interest groups, and monitoring along the production stages are necessary, adding greatly to the monitoring costs (Jahn, Schramm, and Spiller 2005). When it is too costly for outsiders to measure the true performance, it may be profitable for the agent to reduce performance. While firms with good performance can signal their performance to outsiders, the availability of costly signals may be limited, and the result may be that good CSP is not available in the market (Spence 1973).

1.3 Retail contracts and corporate social performance

Following agency theory and the strategic view of CSP, retail chains and stores will produce the amount of social performance that maximizes their profits (Connelly, Ketchen, and Slater 2010). A retail store's and chain's CSP will be decided by the relationship between CSP and profitability for the store and for the chain. Whether good CSP is profitable depends on incentives, monitoring costs, and demand from principals such as customers or regulators. At the store level, incentives to maximize profits vary according to the chain-store contracts, or for independent stores the absence of such contracts. Independent stores have larger financial incentives than chain stores to maximize profits, since the independent store can keep all the additional profit, while the chain store has to forward part of additional profits to the chain. Franchised stores have larger financial incentives than corporate stores to maximize profits, based on the same argument. The effect of the different contracts on CSP will then depend on the relationship between financial profitability and CSP. For issues where CSP is profitable for the store, independent stores have the strongest incentives to produce high CSP followed by franchised stores and finally corporate stores. For issues where CSP is expensive for the store, corporate stores should have better CSP than franchised and independent stores, since they have fewer incentives to reduce quality to increase profits.

The profitability of social performance at the chain level will influence how the chain uses incentives and monitoring towards stores. If CSP is unprofitable for the store but profitable for the chain as a whole, the chain can use incentives or monitoring to influence the behavior of the store. In the extreme case, the chain can use behavioral contracts (corporate stores) to limit the problem of stores reducing quality. As always, this comes at the expense of reduced profitability, since corporate stores are less efficient than franchised stores, and monitoring is costly and difficult. The chain can include incentives for good CSP in the franchise contract, but again at the expense of lower incentives to increase profits, since multiple tasks always come with a cost to performance (Holmstrom and Milgrom 1991). In total, the prediction is that for dimensions of CSP that are profitable for the chain but unprofitable for individual stores, the CSP of corporate stores should be higher than the CSP of franchised stores and independent stores. This is parallel to the free riding problem in franchise studies (Kidwell, Nygaard, and Silkoset 2007) where the store has incentives to reduce quality when this is profitable for the store and monitoring costs for the chain are high.

The levels of information asymmetry are important predictors of CSP. Without information asymmetry, no agency problems exist, since the principal simply can determine the performance of the agent and reward him or her accordingly (Husted 2007; Jacobides and Croson 2001). A retail chain, for instance, can easily achieve the optimal level of CSP in their stores if the two parties share the same information. The same applies for other principals, who can easily observe the level of CSP and reward stores or chain (the agents) that behave according to their preferences. Under information asymmetry the level of CSP will be the level of CSP demanded by principals, at least in the long run. Under information asymmetry, the situation is different. The retail chain has to engage in costly monitoring or the use of corporate stores, which reduces their profits. This may still be the optimal situation if high CSP is demanded. However, high information asymmetry for the retail chain also entails high information asymmetry for customers, who have difficulties assessing store and chain performance. While the firm may signal their performance to outsiders, costly signals are not easily always available, and the result can be that the market for good CSP collapses and only poor CSP is available (Spence 1973; Akerlof 1970).

The agency theoretical model of CSP in retail thus suggests that CSP will be high on dimensions with low information asymmetry that are demanded by outsiders. Under high information asymmetry and little demand, corporate stores should do better than franchised and independent stores, who have incentives to reduce quality. Empirical studies examining the influence of organizational structures in retail or similar industries such as hotels and restaurants on CSP generally support these predictions. Units that are chain members have better CSP than independent units on issues such as CSR activities (Blombäck and Wigren-Kristoferson 2011) and environmental management (Álvarez Gil, Burgos Jiménez, and Céspedes Lorente 2001). These are activities that may be unprofitable at the store level, but that may add to the chain's reputation, and chains therefore chose to implement them, often as a result of outside pressures. Also, independent hotels are more likely to write negative reviews about their competitors than chain hotels (Luca and Zervas 2013; Mayzlin, Dover, and Chevalier Forthcoming), potentially reflecting their higher incentives for doing so. Independent hotels benefit more from the negative reviews since they can keep any additional profits for themselves. Recent empirical studies have also confirmed the free riding problem in franchising by finding that franchised restaurants have lower quality or higher prices than corporate restaurants belonging to the same chain (Jin and Leslie 2009; Ji and Weil 2009; Ater and Rigbi 2013). Franchised units are also more likely than corporate units to pass cars in vehicles emission tests (Pierce and Toffel 2013). Note that the empirical findings on free riding have all been on dimensions of CSP with high monitoring costs for the chain and other outsiders.

The profitability of CSP at the store level also has consequences for the chain. When CSP is unprofitable for the stores and monitoring is expensive and difficult, the chain may choose to reduce investments in common activities to reduce the problems of free riding. A chain might not make strong promises on CSP, for instance, when they fear that they may not be able to implement the desired level of performance at the store level. Further, knowing that other stores have incentives to free-ride, each store may also engage in bargaining to stop such common activities at the store level. Supporting this perspective, some research has found that franchised chains advertise less than integrated chains (Michael 1999) and on average lower quality (Michael 2000). The percentage of franchised stores in a retail chain has also been found to influence negatively the amount of CSR communication from the chain (Perrigot, Oxibar, and Déjean Forthcoming).

1.4 Local market structure and corporate social performance

1.4.1 Competition

Competition may both improve and reduce social performance in general (Shleifer 2004). For dimensions of CSP valued by customers (the principal), such as product or service quality, competition is likely to contribute positively. Competition gives incentives to produce high quality since the customer easily can switch supplier. Routes with more than one airline have fewer delays, arguably an important dimension of product quality in airline services (Mazzeo 2003; Greenfield 2012). Supermarkets with more competition have less inventory shortfalls, and when Wal-mart establishes in an area, the existing supermarkets reduce their shortfalls (Olivares and Cachon 2009; Matsa 2011). A positive relationship between more direct measures of CSP and competition have also been found, firms in industries with tough competition have better CSP ratings and lower toxic emissions (Fernández-Kranz and Santaló 2010; Flammer Forthcoming; Declerck and M'Zali 2014; Hawn and Kang 2013). However, competition and rivalry can also increase cheating and unethical behavior (Schwieren and Weichselbaumer 2010;

Kilduff et al. 2012). Soccer players for instance get more yellow and red cards when playing against their team's rivals (Kilduff et al. 2012), and hotels that have tough competition are more likely to write fake, bad reviews of their competitors (Luca and Zervas 2013; Mayzlin, Dover, and Chevalier Forthcoming).

These findings are not contradictory. When a high level of CSP is demanded by the principals and monitoring costs not excessive, competition is likely to contribute positively towards CSP. Supermarkets reduce their shortfalls under tough competition because customers want to find their favorite products in the shelves, can observe performance easily in the store, and can go elsewhere if the store is sold out. The same basic logic should apply to CSP. If principals do not demand good CSP, or if performance is very costly to monitor for outsiders, competition can lead to worse CSP, as firms can reduce performance to increase profits. As already mentioned, in a study of vehicle emissions tests, (Bennett et al. 2013) find that firms with more local competitors are more likely to pass cars in the emissions test. They suggest that this is due to the pressure of increased competition to give the customers what they want, at the expense of social welfare. Others have named the practice “unethical demand” (Pierce and Snyder 2013). This behavior can take place since the relevant market does not value good social performance (reduced vehicles emissions) and the behavior of the firms testing for vehicle emissions is expensive to monitor for outsiders such as authorities and competitors.

Competition does not necessarily influence all firms equally. As discussed, agency theorists have recognized that the competitive pressures of the market may work as an incentive scheme in itself (Hart 1983). If competition in a market is tough, corporate managers have the incentives to improve the performance of their units, especially since they may be competing with other firms where the owner is also the manager and who therefore do not have the same incentives to reduce effort. The “slack” necessary for the managers to shirk is not available.

In total, competition should increase CSP in retail when principals demand it and information asymmetry is low. In such situations, competition will force firms to provide high CSP. This includes corporate stores, who have fewer financial incentives but will have to provide high levels of CSP to keep up with independent and franchised stores. Under high information asymmetry, competition should decrease CSP, since agents can benefit from reducing quality. In such situations, tough competition will lead corporate stores to reduce their quality not to lose out in the competition with franchised and independent units.

1.4.2 Market size

One potential market solution for problems of unobserved quality is consumer learning and firm reputation (Klein and Leffler 1981; Shapiro 1982; Jin and Leslie 2009). Consumers can learn about the unobserved quality of a product or service by their own experience or from other consumers. This has consequences for the behavior of firms, since it can become profitable to produce good quality even if quality is not directly observable (Brickley and Dark 1987). Repeat customers learn about quality and make it costly to produce low quality since the future income stream of their business will be lost. Similarly, potential customers can learn about a firm's quality from other customers, the media, or expert reviews.

Previous research has focused on the population characteristics of the local market, such as population density or the degree of repeat customers as proxies for the reputation effects (Jin and Leslie 2009; Brickley and Dark 1987). In this study I focus on the size of the local market.

In small geographical markets actors are aware of each other and close relationship exist between firms and customers and between different customers. As a result of the close relationships and the actors' awareness of each other in the small markets, reputation effects are particularly strong (Lepoutre and Heene 2006). Information about the quality of a retail store may quickly be spread among community members. Further, this news can easily be connected to the manager of the store. Empirical studies have shown that small communities rely less on formal governance mechanisms such as formal punishments and more on informal methods (Henrich et al. 2010). A particularly relevant study is McDevitt's (2011) analysis of the impact of reputation in small and large markets. He hypothesizes that firms in small markets are less likely to change their names to get rid of a poor reputation, since customers in small markets will recognize the firm anyway, and that firms in small markets are more sensitive to both good and bad reputations. Studying plumbing firms in and around Chicago he got support for his hypotheses, and found that firms in small markets outside Chicago were less likely to change names in general and more likely to exit or change names following consumer complaints.

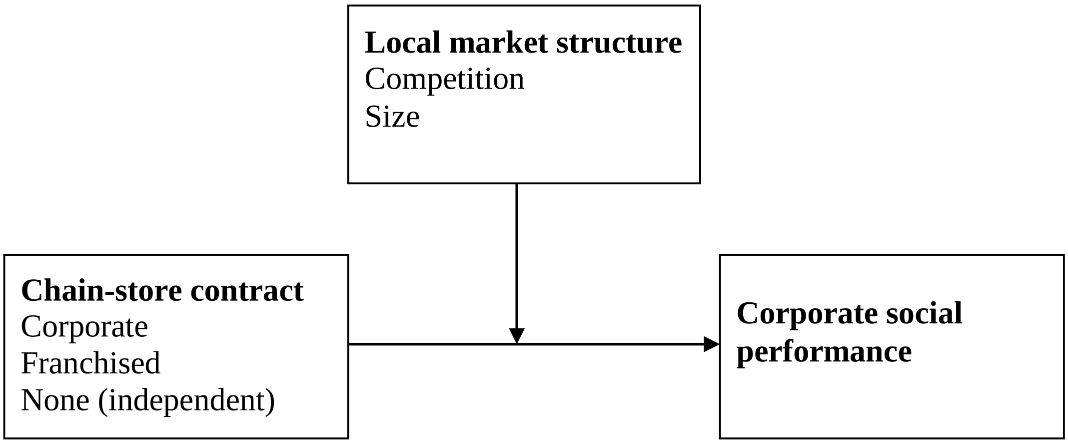
Again, agency theory predicts that the effects of reputation are likely to influence firms differently depending on their organizational forms. Since firm reputation can be a signal of unobserved quality, reputation effects can reduce the problem of free riding by franchisees. In small markets, franchisees have incentives to improve their quality relative to corporate stores since they benefit from a good reputation.

In total, retail stores in small markets should show higher levels of CSP when demanded by principals, even on dimensions of performance with high information asymmetry, as the reputation effects reveal true quality and give firms incentives to improve. Franchised stores have particular financial incentives to improve their quality not to lose out in the competition with corporate stores, and the reputation effects in small markets should therefore reduce performance differences between the organizational forms.

1.5 The research model illustrated

Illustration 1 shows the general research model for the dissertation. The general proposition is that due to the different profit motives at the store level, organizational form will have consequences for CSP, and that this effect will be moderated by the size of and competition in the local market. The specific hypotheses are included in the individual articles.

Illustration 1: The research model



1.6 The relevance of the research

The research aims to improve the understanding of how different types of contracts in principal-agent relationships are influenced by important factors outside the contracts itself, namely competition and reputation. While the articles in the dissertation use the retail sector as an empirical context, agency relationships are abundant in most areas of life (Shapiro 2005). The central choice in agency theory, and in many real-life situations such as employee and CEO compensation, buyer-supplier relationships or public regulation of companies, is between a behavior based or outcome based contract. This dissertation contributes to the understanding by studying factors outside the contract itself that influence the results.

The relevance may be particularly high in retail. In the last decades the trend has been towards more domination of chains over independent stores (Levy and Weitz 2012; Basker, Klimek, and Pham 2010), and the franchise form of organization have grown in popularity (Dant, Grünhagen, and Windsperger 2011). This research will contribute to a better understanding of when the different organizational forms are likely to succeed, and their strengths and weaknesses from the perspectives of both the firm and society. Since the beginning of franchising there have been discussions about potential negative effects, but concerns have mainly been about unequal power relationships between franchisors and franchisees (Hunt 1972; Storholm and Scheuing 1994). However, there may be other effects that also should guide chains in their choices of organizational form and governments in their design and implementation of laws and regulations.

It is also important to understand the drivers of social performance in the retail sector. The retail sector is a large and important part of the economy with a considerable impact on the society. In Norway, where the data for two of the three articles in the dissertation comes from, the retail sector makes up for around 10% of GDP (Statistics Norway 2013a) and employs around 370 000 people in more than 53 000 firms (Nygaard and Utgård 2011). Retail firms are the middlemen between producers and consumers, and can influence both. The determinants of CSR in retail are important to understand from a societal perspective, since retailers link the final consumers with suppliers and producers, translating the interests of the consumers for CSR into pressure upstream in the supply chain (Ytterhus, Arnestad, and Lothe 1999). Large retailers also have considerable power in the relationship with its suppliers, sometimes so much that it raises concern about the well-being of other actors (Bloom and Perry 2001), and it has been suggested that retail chains are in practice creating their own private standards regarding CSR (Fuchs, Kalfagianni, and Arentsen 2009).

1.7 The articles in the dissertation

The dissertation consists of three independent articles, testing parts of the theoretical model in different contexts and with different data. In the first article ("Franchising, local market characteristics and alcohol sales to minors in retail") I study how the organizational form of the retail store interacts with competition, the risk of sanctions, and market size to influence the store's social performance. This is the most complete test of the main research question in the dissertation. As a measure of CSP I use alcohol sales to minors, which previous research have found to be relatively common, despite being illegal. The data for alcohol sales is collected by underage teens as mystery shoppers, and is combined with data about the local market and an extensive set of control variables collected from a range of other sources.

In the second article ("Market structure, chain membership and food hygiene in retail") I study the influences of chain membership and competition on food hygiene in supermarkets. Previous research has generally found a positive relationship between competition and quality. I hypothesize a U-shaped relationship, where low and high levels of competition give better quality, since stores with little competition are located in small markets with strong reputation effects that also can influence quality positively. I further hypothesize that chain stores are less sensitive to competition, since chains to a large extent standardize store quality. The data about food hygiene quality comes from the Danish veterinary and food administration who regularly inspects all firms that sell food. The results of the inspections are published both outside the supermarket and online, making it easy for customers to evaluate quality.

In the third article ("Retail chains' corporate social responsibility signaling") I study how the retail chain's organizational form influences its CSP signaling on its web pages. I hypothesize that vertically integrated chains are more likely to signal CSP than franchised, plural and voluntary chains, since these chains have larger problems getting their stores to commit to common investments in CSP and CSP signaling. I also include other hypothesis testing signaling theory. The data is based on a content analysis of the web pages of 208 retail chains in the Norwegian market, combined with information about the chains collected from other sources.

Table 2: Overview of the articles

Article	**Key IVs**	**Moderators**	**DV**	**Data**
Franchising, local market characteristics and alcohol sales to minors in retail	Franchised vs corporate store	Competition Market size Risk of sanctions	Alcohol sales to minors	Alcohol sales data collected by underage NGO members. Other variables collected from a range of sources.
Market structure, chain membership and food hygiene in retail	Chain store vs independent store	Competition Market size	Hygiene inspection score	Data from Danish veterinary and food administration on hygiene inspections of supermarkets.
Retail chains' corporate social responsibility signaling	Chain organizational form		CSR signaling on web page	Data set with 208 chains from the Norwegian market. Content analysis for CSR signaling, other variables collected from secondary sources.

The papers of this dissertation (pages 21-86) are not available in BI Brage, due to copyright matters:

Paper 1:
Franchising, local market characteristics and alcohol sales to minors in retail

Paper 2:
Market structure, chain membership and food hygiene in retail

Paper 3:
Retail chains' corporate social responsibility signaling

5 Summary and conclusions

The main purpose of this research has been to study how retail chain contracts influence corporate social performance (CSP) and how this effect is influenced by local market size and competition. High levels of CSP can be profitable for firms when customers or other groups value it, but unprofitable when not demanded or difficult to observe. Agency theory suggests that retail firms will produce the level of social performance that maximizes their profits. The financial incentives of individual stores depend on the chain-store contract, and this dissertation has therefore examined empirically whether performance varies between contracts. Further, agency theory suggests that competition and reputation can give agents incentives to produce high quality regardless of the organizational form (Hart 1983; Shapiro 1982), thereby reducing performance differences across contracts, This dissertation has provided empirical tests of these predictions.

The dissertation has consisted of three independent empirical articles testing different aspects of how contract choice influences CSP. Two of the articles have also tested the moderating effect of local market competition and size. The first article ("Franchising, local market characteristics and alcohol sales to minors in retail") studied how chain-store contracts (corporate or franchised store) interact with competition, the risk of sanctions and market size to determine alcohol sales to minors in retail stores. The second article ("Market structure, chain membership and food hygiene in retail") studied how chain membership interacts with competition and market size to influence food hygiene in retail stores. The third and final article ("Retail chains' corporate social responsibility signaling") studied how retail chains' organizational forms differ in their corporate social responsibility signaling.

5.1 Findings

5.1.1 Retail contracts and corporate social performance

The effect of the chain-store contract on CSP was tested in all three articles. The first article examined the difference between franchised and corporate stores, the second article the difference between chain stores and independent stores, and the third article the difference between different types of chains at the chain level. As hypothesized I find that corporate stores have better social performance than franchised stores in the case of alcohol sale to minors. In the second article, where I did not have a clear hypothesis, I find that chain stores have better social performance (measured as food hygiene quality) than independent stores under medium levels of competition. Under low and very high levels of competition, independent stores have the same social performance as chain stores. In the third article, studying CSP at the chain level, I find that vertically integrated chains have significantly higher CSP than franchised chains, and marginally better CSP than plural and voluntary chains. In total, agency theory is fully or partly supported for the direct effects of organizational structure on CSP in all three articles.

5.1.2 The moderating effect of local market structure

The potential moderating effect of the size of and competition in the local market was examined in the two first articles. In the first article I find no influence of competition on the effects of the different contracts on alcohol sales to minors. My hypothesis was that corporate stores would behave more like franchised stores under tough competition, since tough competition gives corporate managers incentives to be efficient to avoid being run out of business. I do not find any effect of competition when using the number of competitors in a radius of 500 meters as the measure. When using other measures of competition such as the Herschman-Herfindahl index or number of stores in the zip code (see the appendix to the article), franchised stores are more sensitive to tough competition than corporate stores, contrary to the predictions of agency theory.

In the second article, I find that competition influences food hygiene more for independent stores than for chain stores in most models. This is as hypothesized, since retail chains standardize the behavior of their stores to some degree, and the individual stores therefore have less freedom to adjust to the local market situation.

Both the two first articles investigated the moderating effect of small markets on different types of contracts. In the first article, I find that stores in small markets are less likely to sell alcohol to minors, and that corporate stores are influenced more by the small market than franchised stores. Again, this is contrary to my hypothesis and the predictions of agency theory. In the second article, I find no significant differences between independent stores' and chain stores' responses in small markets. This is as implicitly predicted, since the information asymmetry is low and customers and chain managers relatively easy can monitor store performance.

In total, agency theory is not supported when it comes to the moderating effects of the local market structure.

5.1.3 Other findings

All findings on variables not included in the main research model are reported in the individual articles, but some findings deserve special discussion. One moderating variable examined in the first article was public monitoring and sanctions. I find that franchised stores are more influenced than corporate stores by the risk of sanctions by the local municipality. This is as hypothesized, and consistent with a theory where franchised stores are more concerned about the possible financial losses from losing their sales permit for a period than corporate stores, thus supporting agency theory.

Previous empirical research has found varying effects of competition on CSP, as predicted by agency theory (Matsa 2011; Bennett et al. 2013). When performance is demanded by the principal and monitoring costs are not too high, competition typically increases quality In my second article I partly find the same effect, supermarkets under tough competition have better food hygiene. Note however that the effect is U-shaped and negative for most levels of competition. Other studies have found that increased competition also may reduce CSP when information asymmetry is high (Bennett et al. 2013). I do not find robust evidence of this in article 1, competition has no direct influence on CSP, but in some models estimated as robustness checks competition increases the likelihood of franchised stores selling alcohol.

In both articles 1 and 2, stores located in small markets have better CSP than stores in larger markets. They are less likely to sell alcohol to minors, and they have better food hygiene than stores in larger markets. This is as hypothesized, as small markets have strong reputation effects.

5.2 Theoretical contributions

5.2.1 Agency theory

The largest theoretical contribution of the dissertation is the examination of the performance effects of chain-store contracts under different market structures. Agency theory suggests that competition can reduce agency costs, since the market works as an incentive scheme itself by putting pressure on inefficient actors. In the context of retail chains, this should make corporate stores more efficient, since they risk going out of business if they do not keep up with their franchised or independent competitors. This prediction has previously been tested with the decision of whether to use franchised or corporate stores as the dependent variable (Nygaard and Myrtveit 2000), but this study is the first to test the actual performance effects of competition on different contracts. In article 1, I find no effect, and thus do not get support for agency theory, as competition has no effect on alcohol sales for either franchised or corporate stores. In article 2, I find that chain stores have similar levels of food hygiene as independent stores at high levels of competition. In low levels of competition the theory would predict better hygiene for independent stores, but I do not find this, since stores at low levels of competition have similar levels of hygiene. I argue that this is a result of the small markets securing good quality. In the setting of the Danish food hygiene scheme the monitoring costs for the retail chain are low due to the Smiley Scheme. It is therefore not clear how much slack corporate managers in reality have.

Another contribution is showing how small markets can reduce agency costs. Previous studies have suggested that larger markets have lower agency costs because monitoring is relatively cheaper and competition tougher (Brickley and Dark 1987). I hypothesize and find in two of the studies that small markets reduce agency costs for the principal. Stores in small markets have better food hygiene and lower probability of selling alcohol to minors. My explanation is mainly that the reputation effects are particularly strong in small markets. The importance of reputation has been recognized in agency theory (Jin and Leslie 2009; Shapiro 1982), but this has not directly been connected to the market size. I also argue that franchised stores should improve their performance relatively more in small markets, since the reputation effect is equally or more important for them, but I do not get support for this.

Finally, the potential for franchised stores of free riding on the chain reputation has long been recognized theoretically, but only a few studies have shown the effect in convincing manner (Jin and Leslie 2009; Ji and Weil 2009; Pierce and Toffel 2013). This study confirms these findings in article 1, and is the first to empirically show free riding in the retail sector, as the previous studies have all been in the restaurant sector.

5.2.2 Other theories

Some findings in the dissertation also contribute to other theories and fields. The marketing dyad environment framework by Achrol et al. (1983) recognizes that the environment around the dyad will influence both structure and processes within the dyad. The framework includes competitors and regulatory agents as two important groups of actors with impact on the focal dyad. This research has confirmed the influence of both groups, and shown that competition can reduce agency costs for the chain in the retail chain-store dyad. It has also shown that regulatory agents, such as the local municipality with their monitoring and formal punishment, and small markets, can influence the outcomes of contract choice in the dyad. Overall, the findings give some support to the marketing environments framework.

The dissertation also contributes to the understanding of the importance of the local market as a governance mechanism in retail. Retail stores have a specific geographical location. The importance of adjusting the quality and product offerings to the local preferences has long been understood, but this dissertation also illustrates how important the local market is in governing social performance.

The dissertation contributes to a recent and growing literature on the relationship between competition and quality. Several studies, also in retail, have found a positive relationship between competition and quality when quality is important and visible (Matsa 2011; Olivares and Cachon 2009), but a negative relationship when quality is difficult to observe (Bennett et al. 2013; Mayzlin, Dover, and Chevalier Forthcoming). This dissertation gives partly supporting evidence for the differential effects of competition, which improves food hygiene under low information asymmetry, but does not influence alcohol sales.

A final contribution is to the growing literature in the field of forensic economics, which is the field where economic methods are used to detect and understand behavior that the parties involved in would prefer to keep hidden (Zitzewitz 2012). Alcohol sales to minors is such a behavior, and while in line with several other articles (Jin and Leslie 2009; Zinman and Zitzewitz 2012) the first article in this dissertation finds that the financial incentives influence the likelihood of economic actors to engage in unethical or illegal activities, the article contributes by showing how market structure can moderate this effect.

5.3 Practical implications

Managers of retail chains should be aware of the influence their organizational form has on social performance. The potential for free riding among franchised stores have long been recognized theoretically, and recent empirical studies have confirmed the problem. This dissertation confirms that free riding is a problem, and that even if retail chains are aware of the problem, they do not manage to curb it with monitoring or appropriate contracts. A natural managerial implication is to either invest more in monitoring, or structuring contracts differently by for instance including financial punishments if a store performs poorly. If chains increase monitoring or add sanctions, costs will increase, and the chain will have to trade off better performance versus increased costs. If agency costs become large enough, it will at one point become more profitable to use corporate stores.

Retail chain managers should also notice the (lack of) impact of competition and market size on the performance of their stores. Agency theorists have suggested that competition can work as an extra incentive for corporate managers, but I do not find evidence of this. Competition improves hygiene, but more for independent stores than chain stores, and if there is any indication about competition increasing alcohol sales for minors, it is for franchised stores, not corporate stores. Taken together with previous research which has also not found any influence of competition, chain managers should not rely on market competition to discipline their managers. On the other hand, there are good reasons for retail chain managers to rely on the governing effects of small markets, which can improve quality considerably.

The findings can be used by public authorities when designing their policies and monitoring strategies. Both the Norwegian alcohol sales monitoring and the Danish food hygiene monitoring system is generally based on annual inspections. However, the respective authorities can freely decide on any further inspections, meaning that they can take local market characteristics into consideration. Based on the findings in this dissertation they should divert resources from corporate to franchised or independent stores and from small to larger markets.

5.4 Limitations and future research

One of the limitations of the dissertation is its reliance on observational and secondary data. The data has many strengths, it is for instance unlikely that all stores would answer honestly if you asked them about whether they sell alcohol to minors (Mick 1996), and the use of observational data reduces this problem. On the other hand, secondary data has limited ability to provide insight into the precise mechanisms or processes that takes place in the store. For the mechanisms of free riding or the perceived pressures of the market, I rely on theoretical arguments. In reality, I cannot rule out alternative explanations. There may for instance be differences in the objective levels of competition and how managers perceive competition (Gripsrud and Grønhaug 1985), with consequences for store performance. Some measures used in the studies are not ideal and can be improved in future studies by collecting primary data. In particular I have in mind the measures for private label use and low price strategy in article 3. Primary data from the chains about their pricing and brand strategies could have given more valid results, but were costly to collect.

In general, the articles are based on cross-sectional data with the usual limitations about establishing causal effects. While I use words such as “influence” or “effect”, in reality the findings are correlational, and I cannot make causal claims. A general problem in the studies is the risk of biased estimates due to endogeneity, which is the potential correlation between the error term and the independent variables in a regression model (Sande and Ghosh 2014). Endogeneity can be caused by omitted variables, simultaneity or measurement errors. Solutions to this problem are generally experimental or quasi-experimental methods, including panel data methods (Wooldridge 2009). In the two first articles I have partly longitudinal data, but due to the data structure and my variables of interest pooling the data was the best option. One illustration: In the first article, only a couple of the stores changed organizational form between corporate to franchise during the period. I could therefore not use the variations over time to estimate the effects of organizational form. Similarly, the data set for the second article does not identify changes in competition in the period. Using econometric methods for panel data would therefore not have helped my analysis. The best option would likely have been to use instrumental variables techniques (Sande and Ghosh 2014; Wooldridge 2009). Such techniques use an instrument that is correlated with the independent variable but not directly with the dependent variable. The challenge is to identify relevant instruments. Previous studies in franchising (Kosová, Lafontaine, and Perrigot 2013; Ji and Weil 2009) have used the percentage of franchised units in the local market as an instrument, based on the logic that the cost of monitoring is reduced if there are more franchised stores in an area. It is unclear how good this instrument in reality is, since it is not clear what influenced the organizational form of the first store, or how well this would work in the Norwegian context with many small markets. Future studies may still want to use instrumental variables to control for the endogeneity of organizational form.

Throughout the dissertation I have emphasized the role of the financial incentives at the store level as the cause of the differences in CSP between franchised and corporate stores and chains. Exactly how the financial incentives shape the behavior of stores is not clear. It may be that franchisees are directly motivated by the monetary incentives to maximize profits by for instance cutting costs and reducing quality. Alternatively, franchisees may differ from corporate managers in their personal values, perhaps being more concerned with financial profits and material benefits and less concerned with the well-being of others. There is some empirical evidence on the differences between entrepreneurs and employees supporting such a perspective, entrepreneurs may for instance be more action-oriented with some negative consequences for ethical considerations (Harris, Sapienza, and Bowie 2009). Franchising contracts also work as selection mechanisms, where only those who believe that they have the qualities to succeed become franchisees. This means that they may be systematically different from corporate managers even within the same chain. The incentives of franchising still cause differences in CSP, but the mechanism is different. Performance differences may be a result of both selection and incentive effects, and only data about managers' personalities and values could answer which of the mechanisms is at work. This is an interesting avenue for future research.

I have argued, and found empirical support for, that small markets can improve quality. My theoretical explanation is that reputation effects, which can reveal quality also when quality is directly unobservable, are particularly strong in such markets. Again, I cannot completely rule out competing explanations. Firms in small markets may be more embedded in the community, being more concerned with the well-being of their customers and other community members. Firms in small markets may have access to a more stable work force, reducing training and monitoring costs and increasing quality. In the case of alcohol sales, if the work force is more stable workers may also be older and may find it easier to ask customers for ID. While I have tried to control for some of these alternative explanations, in particular by including market dummies in article 2, future studies may want to use more and other proxies for reputation to further establish the effect.

One of the big discussions in the literature on CSP is the relationship with financial performance. This dissertation has focused only on CSP, mainly due to data limitations. It would be a contribution to examine the relationship between CSP and financial performance at the store level, using behavioral data, and not the typical reputation/rating data used in the CSP-CFP studies. The main challenge here is the data access; financial data at the store level is generally not publicly available since the chains only report at the group level. The exception is franchised stores, which have to report publicly since they are independent firms. A realistic future project is to combine the data on alcohol sales to minors with financial data for the franchised stores, to examine whether the financial situation is correlated with CSP.

All three studies have used single indicators of corporate social performance as their dependent variables. CSP is a broad term covering different aspects of firm behavior, and the correlation between them is not obvious. Devoting more resources to one aspect or dimension of CSP gives less available resources for other aspects. This is the essence of the literature on multi-tasking in agency theory (Holmstrom and Milgrom 1991), which predicts that agents will shift efforts to those aspects that are easily observable. The prediction from this literature would be that for instance introducing the Smiley-scheme would make stores devote more efforts to food hygiene but potentially less resources for other aspects with uncertain consequences for total CSP. Empirical studies on CSP show mixed findings on this, Matsa (2011) found that several dimensions of store product and service quality was positively correlated, while Propper et al. (2008) found that competition influenced hospitals to reduce waiting times (easily observable) but decrease treatment quality (difficult to observe). To avoid or at least reduce this problem I would need information about several aspects of CSP, which was not available to me.

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