Pattycake - Pattycake: Who is to Bake?

For most of its 46-year history, the making of doughnuts was done at each Tim Hortons (http://www.timhortons.ca) outlet by a local staff. However, there were two problems with this approach: (1) the difficulty of attracting a baker to come to work in the early hours of the morning and (2) the lack of inter-store product consistency. In order for there to be a batch of fresh donuts for the morning crowd, bakers had to come in at 3:00 a.m. to start preparing the morning delicacies; this was not an exciting time to start work. The other problem was the varying size of donuts across outlets. Sometimes the customer would get a big donut, but at other times, at the same or different outlet, the same style of donut was smaller. The varying size was due to the human element.

In 2003, Tim Hortons thought it had resolved both issues. A joint venture was formed with a Swiss-owned company (IAWS Group Ltd.) that involved the development of a factory in Brantford, Ontario (about 100 km west of the Oakville, Ontario, head office, that would par-bake and flash-freeze all of the donuts, pastries, Timbits, and bread products. The various products would then be shipped out to the over 3,000 outlets in the primarily franchised system, where final baking and product finishing would take place. Each outlet was required to invest over $30,000 in new technology that would complete the baking of the donuts and related items. Final finishing (e.g., glazing, chocolate coating) would take place at each local outlet. Diehard donut lovers were not pleased with this change, particularly, since the company maintained its "Always Fresh" motto.

In early 2010, the foreign partner indicated that it would no longer continue as a partner in the current structure of the operation. A clause in the agreement between the two companies gave Tim Horton the option to buy out the 50% share of the joint venture owned by the foreign partner or to sell its share in the company.

Because of the essential nature of the product-supply component in Brantford to the Tim Hortons operation, it is expected that the company will make an offer to buy out its foreign partner. However, because of the essential nature of this component of the channel, it also is expected that IAWS will ask a high price for its share of the business.

The advantage of the new approach to product supply is that each outlet can easily adjust to local demand needs with a "fresh" product and minimize waste through better inventory control. The need to high a fully-qualified baking staff is also minimized, since an almost finished product arrives at each outlet; just the finishing touches are required. The structure of transportation costs also changed drastically with the centralized supply point for a further-prepared product.

The immediacy of a buyout decision for Tim Hortons has not yet reached the critical point. As indicated, the company can buy out its partner. Another option is find an alternative baking arrangement. In either case, the joint venture agreement provides either party supply rights for seven years after either party shows a desire to end the agreement; thus, Tim Hortons could still have a product-supply chain for donuts and Timbits for a number of years to come, giving it time to consider other options.

Since the franchisees are the only customers of the joint venture, their views on the issue are also important. They already had to financially invest in the technology to adapt to the new product-supply approach; many of whom were not pleased with having to do so.

There is also the possibility that the foreign partner might acquire Tim Hortons' share in the joint venture. Whether or not this is likely to occur, given that its partner, Aryzta AG, is a Swiss Food conglomerate, is actually less important than losing control of its product-supply channel.

In the most recent time period, Tim Hortons has expanded its store operation in the U.S., including New York City. It has plans to expand in Canada, Europe, and the U.S., particularly, in Michigan, not only with respect to its "restaurant" operation but also with respect to the offering of ice cream (Cold Stone Creamery). It also has been successful in warding off an attack by the free-coffee offer by McDonald's in both Canada and the U.S., enabling it to still hold the leading market share in operations of its type, at least in Canada. Nonetheless, one cannot forget the power of the overall, more ubiquitous, coffee and donut market leader, Dunkin Donuts (http://www.dunkindonuts.com).

The details of the ending of the joint venture agreement between Tim Hortons and IAWS are available in a May 13, 2010, news release by the Swiss partner on the following company web site:

http://www.iaws.ie/news-and-media/result-page.aspx?ResultPageURL=http://cws.huginonline.com/A/142194/PR/201005/1415467.xml

The news release indicates that ARYZTA AG announced, through its subsidiary, IAWS Group Limited (IAWS), that notice was given to Tim Hortons that IAWS was invoking the buy/sell provision set out in the 50-50 partnership agreement under the Maidstone Bakeries joint venture. Under this agreement, Tim Hortons can either sell its interest or acquire the interest of IAWS in the joint venture. The reason given by IAWS for the decision was that a different structure of ownership would better serve the interests of the business covered under the current joint venture.

Focus: Franchise system; franchisor; franchisee; joint venture; backward vertical integration; forward vertical integration; conflict; exercise of power; types of power (reward, coercion, expert, legitimate, referent); product density; specialization and division of labour; physical supply vs. physical distribution; attitude; market development; scrambled merchandising; inter-type competition (conflict); intra-type competition (conflict); diversification; market penetration; CERTS (competition, economic, regulatory, technology, social [culture, political, etc.]); hedonic and functional utility; consumer goods - product perspective (convenience good [staple, emergency, impulse, unsought]), shopping good [homogeneous, heterogeneous], specialty good; institutional approach to store classification (convenience store, shopping store, specialty store [specialty store, limited-line specialty store, super-specialty store]).

Questions:

1. Define each of the concepts listed above.

2. What is meant by par-bake? How is this approach and the final "finishing" at the local outlets inconsistent to the "Always Fresh" motto?

3. Explain how the joint venture in a baking operation by Tim Hortons considered to be an illustration of backward vertical integration. What are the advantages and disadvantage of such an operation?

4. Why does an organization use a franchise system instead of direct ownership?

5. Of what benefit is the acquisition of a franchise operation to an entrepreneur? What are the disadvantages of entering such an agreement versus setting up one's own business?

6. What type of conflict exists in the current situation?

7. What type of power does each member of the joint venture agreement have in the situation identified? Explain.

8. If Tim Hortons were to take over the entire Brantford baking operation, what channel concept applies? If IAWS were to take over the entire Tim Hortons operation, what channel concept applies?

9. What ubiquity exists in a baking operation, whether the baking is done locally or at a central location?

10. What is the nature of shipping baked goods versus shipping the raw materials (i.e., ingredients) needed for baking in terms of product density?

11. Explain how inventory control is better achieved by using a centralized baking system?

12. From the perspective of specialization and division of labour, why is the centralized baking approach better for the company? How is this approach not better for the customer?

13. Explain how the concepts of physical supply and physical distribution apply to the original approach of baking from “scratch” at each local outlet versus using the centralized baking approach. How would have things changed?

14. Based on the information provided in the case, explain how the concept of attitude is relevant.

15. Explain how the concept of market development applies in this case.

16. Explain how the concept of scrambled merchandising applies in this case.

17. Explain how the concept of intra-type conflict applies to this case.

18. Explain how the concept of inter-type conflict applies to this case.

19. Explain how the concept of diversification applies to this case.

20. What evidence in the case suggests that Tim Hortons has an objective of increasing the level of market penetration of the company?

21. The acronym CERTS can be used to represent the different aspects of the external environment. Explain which and how the identified components are relevant to this case.

22. Donuts and related pastries are classified primarily as consumer goods. Explain how such products would be further classified as an impulse convenience good from a product perspective.

23 In what way would donuts and related pastries satisfy hedonic and functional utility?

24. Explain how donuts would be classified under the consumer goods classification.

25. Under the institutional approach to store classification, how would an operation like Tim Hortons be classified? Explain.

Note. The majority of the facts presented in this case were drawn from the following sources: [1] Willis, A. (2010, May 14). Trouble in the kitchen at Tim Hortons. The Globe and Mail. Retrieved http://www.theglobeandmail.com/globe-investor/markets/streetwise/trouble-in-the-kitchen-at-tim-hortons/article1568679/ [2] Strauss, M. (2010, May 14). Future of Tim Hortons' baking system uncertain. The Globe and Mail. Retrieved from http://v1.theglobeandmail.com/servlet/story/RTGAM.20100514.escenic_1569626/BNStory/Business/MARINA+STRAUSS