Dedication

To Sophia, Joseph and Polya
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Foreword

Service Franchising: A Global Perspective

Twenty years ago I was offered the position of assistant director of development for the International Franchise Association (IFA). At the time, I knew little about trade associations and even less about franchising, but the job seemed intriguing and the IFA was willing to take a chance on me. Little did I know this would propel me down a path dedicated to one of the most successful models for retail development ever created—franchising.

My first job at the IFA was to meet with franchised companies to learn about the challenges they faced in building their businesses and to sell them IFA memberships. Later, I created the international division for the IFA with the goal of helping members franchise outside the United States. At that time there had been little serious research, or useful writing on international franchising. I learned by observing, listening and working with franchisors as they pursued international franchising. When I was offered a position to help build the international division of a franchised company, I jumped at the chance. For the next fifteen years I learned firsthand the extraordinary power of the business format franchise model.

What I learned was that it is not easy to build a business. It is even more difficult to build a business in the retail sector. The expenses of marketing, real estate, labor costs and rapidly changing consumer habits are just a few of the factors that add to the risk and complexity of this business sector. Trying to replicate the success of a retail concept in a new country creates an even greater challenge. Now the business needs to learn how to operate in the new country with different legal and tax codes, consumer habits, labor laws, retail environment—no easy task as demonstrated by the numerous failed attempts.

It was exciting to experience how the use of a business format franchise system helped reduce the risk for all parties and increase the chances that the venture would be successful. The risks are reduced because the franchisor is transferring specific knowledge about management of the business to the franchisee (or master franchisee). But it is not just a one way relationship where the franchisor has all the answers. Because the franchisee is providing virtually all the capital to build the business, a unique relationship is created where the franchisor must listen and respond to the concerns and issues of the franchisee differently than if that franchisee were simply an employee of the organization. The right franchisee brings critically important local knowledge and experience to the relationship that accelerates the learning curve for the US franchisor. It is the franchisee that is in direct, daily contact with the customer and listening to what is happening on the line level.
This vital information sharpens the franchisor’s awareness of changes in consumer needs, and enables a timely response to keep the product or service relevant.

It is important to remember that franchising is not an industry. Franchising is a business strategy for delivering a product or service to a customer. The IFA has identified over 75 different industries that use the methodology of franchising. According to the 2004 study sponsored by the International Franchise Association Educational Foundation and conducted by the National Economic Consulting Practice of PricewaterhouseCoopers, in the United States alone, more than 760,000 franchised outlets employ more than 18 million people providing nearly 14% of US private-sector employment. This generates $1.53 trillion in economic activity or nearly 10% of the private-sector economic output. Outside the United States franchising appears to be growing at an even faster pace.

At a time when use of this powerful business model for growth is expanding around the world, it is curious that there has been relatively little academic interest in the subject. Without empirical research it is difficult to evaluate the impact that franchising is having in a country. Again, franchising is not an industry, so the overall effect of the franchising model on an economy is hard to measure. Because franchising has been dominated by the fast food industry, many policymakers focus on the product rather than the model that franchising is and how it facilitates the transfer of best of business development strategies and processes. A successful franchise system teaches standardization, training, marketing, operational support—key areas that improve the competitiveness and development of a robust retail sector. It is not often understood that franchising creates important opportunities for local investment and employment. If policymakers better understood the positive impact of franchising on local and national economies and societies, particularly in emerging markets, then we might see a more supportive regulatory environment, one that works to nurture and protect the development of franchising as a business model. Ilan Alon’s work examines the total impact of international franchising, and specifically the implications for emerging markets. He provides is an important addition to this sparsely covered topic.

From the US franchisor’s perspective, many attractive opportunities encourage the franchisor to venture into markets beyond the United States. However, I have learned from direct experience the hardships and challenges that must be overcome in order to make a franchised business successful outside of the US. Most franchisors start with the strategy of finding the right local partner, or perhaps more accurately, the local partner finding them. They then embark upon the process of replicating the key elements of their franchise system and transferring them to the new franchisee. They must adapt the business model to local consumer habits and business customs. While at the same time they must make sure that there is enough capital in the
enterprise to keep the cash flow of the business positive until franchise sales and the ongoing royalty becomes self-sustaining. These are complex and critical tasks that the franchisor must manage no matter which country he begins operations.

But there are key factors that can profoundly influence whether it even makes sense to begin in a certain country. The more knowledge that the franchisor has of the key factors, the more likely will be that company’s success. With this book, Dr. Alon helps the franchisor to ask the right questions to determine whether a company is prepared to tackle risks and realize the rewards associated with doing business internationally.

Franchising is a business model that is becoming even more important in the 21st century. More and more countries’ economies are dominated by the service and information sector. This is a sector ideally suited for the use of franchising. Today the influence of global brands reaches to furthest corners of our globe. Around the world technology continues to transform the way in which we live our lives and conduct our businesses. I have been amazed at the positive impact that use of technology has had in facilitating and dramatically reducing the cost of managing the complete transfer of a business system and the ongoing support required by the structure of franchising. Because of the scarcity of empirical research on international franchising, the knowledge gap is filled with anecdotal information that may or may not be accurate. Dr. Alon’s work makes a significant contribution to the understanding of franchising as a powerful business model in international markets, and it is my hope that more academicians will recognize franchising as a topic worthy of serious research both as a strategy for expansion and as a method of development for emerging markets.

Peter D. Holt
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2005
Preface
Service Franchising: A Global Perspective

The roots of franchising are lost in antiquity. Some argue that English pubs were the first franchises when they were required to be licensed by the king in order to ensure that they met standards for the safety of travelers. Others contend that the original franchisor was the Roman Catholic Church, authorizing parish priests to collect tithes and remit a portion to the Pope. Regardless of whatever the starting date might have been, the global explosion of franchising is barely a generation old.

The growth of franchising has been truly remarkable. Few places in the world have not been touched by this organizational form. While critics attribute homogenization of cultures and economies to aggressive international franchising, the efficient distribution systems, business ownership opportunities, and contributions to society through employment and taxes are undeniable. Additionally, franchisors have proved themselves capable of thinking globally but acting locally by adjusting their product and service offerings to local markets.

But what do we know about franchising? Authors of books and articles about franchising come more frequently from practitioners than from objective researchers. Pioneers such as William Rosenberg of Dunkin’ Donuts and Dave Thomas of Wendy’s published their autobiographies, giving their views from personal experience. The point of academic research is to avoid personal biases by using an impersonal lens in examining how franchising works. It is here that Ilan Alon is making a critical contribution.

Alon has made major contributions to our understanding of franchising, both through his own research and through his compilations of studies by other scholars. Early studies of franchising were predominantly domestic investigations in English-speaking regions, North America, the United Kingdom, and, more recently, Australia. Alon pioneered research into the internationalization of franchising with his dissertation at Kent State University, then, in collaboration with Dianne Welsh, published studies from Asia, Europe, Latin America and other parts of the world.

This book represents a natural extension of his work to date. Here he has organized the best of what studies have documented about successful franchise operations. Alon succinctly extracts from observations about international franchising from both the scholarly and trade literature. Along with these citations, he adds insights that he has gained through research and experience. As a result, we have a book that advances the body of knowledge on international franchising for the academic community. This enables educators to provide high quality information to students and other audiences.
The book also contains guidance for franchisors and franchisees in their efforts to achieve success in the global marketplace, particularly through the case studies of Kodak and Marks & Spencer. Finally, Alon acknowledges that public policymakers are giving ever greater attention to franchising. This book provides factual information for those concerned with legislation and regulation of franchising. Whichever group you are in, to know franchising, you must have a global perspective.

Frank Hoy, Ph.D.
El Paso, Texas, USA
2005
Acknowledgements

This book is a product of over nine years of research on the subject of franchising, leading to numerous articles, books, and presentations on the subject. Collectively, the chapters of this book integrate much of my research on franchising as a global phenomenon.

It is needless to say that many people and organizations have been instrumental in my professional development and franchising research leading to this point. But, an acknowledgement of select contributors is worth mentioning. Key among them, of course, are my parents, wife, family, mentors, friends and colleagues. This book is dedicated to my family.

Franchising was introduced to me through Dr. John Ryans, a longtime Kent State University faculty member in international business and marketing and James R. Good Chair of Global Strategy at Bowling Green State University. It was Dr. David L. McKee Professor of Economics at the Graduate School of Management of Kent State University who supported, encouraged, and endured through my years of dissertation research, which led me on this path.

The path of franchising research is truly and fruitful one. Franchising has been largely developed by niche researchers who cut across the traditional disciplinary divides (e.g., marketing, management, law, economics, finance, international business, and entrepreneurship). Organizations such as the International Society of Franchising (ISOF), in particular, and USASBE, more generally, have united these researchers leading to new research interactions. I am particularly thankful to the various organizers of ISOF for showing the relevance and advancing knowledge on franchising globally.

Also, the following organizations have to be acknowledged: Blackwell Publishing, Sage Publication, St. Luis University, Journal of Business & Entrepreneurship, Academy of Marketing Science Review, and Thunderbird International Business Review for earlier versions of some chapters.

I would also like to thank my colleagues and co-authors namely Ralph Drtina, James Gilbert, David McKee, James Johnson, Noora Anttonen, Mika Tuunanen, Mark Munoz, and Igor Pavlin for having patience, working under pressure, and for their singular contributing to the emergent field of franchising. Included in this group of respected contributors are foreword writer Peter Holt, an executive and veteran of the industry, and the preface writer Frank Hoy, an influential franchising author. Their full biographical sketches are included in the back of this book.

Finally, we would like to thank Springer, the publisher, and, in particular, Sean Lorre, the editor, for showing flexibility and propelling the process of publishing this book.
I. Franchising Development
Chapter 1
Introduction

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In recent years, a plethora of articles have emerged discussing franchising in a global context. A basic search (conducted on June 9, 2005 by the author) on “international franchising” using the popular database of ProQuest Direct revealed 123 publications. However, only 25 of the 123 (about 20%) were in scholarly journals. Franchising World, World Trade, International Marketing Review, Hotel and Motel Management, Nation’s Restaurant News, Nation’s Business, and Success were the most relevant publications associated with the search. Of these, only International Marketing Review is a refereed journal. In the same fashion, recent years have also seen an increase in the number of scholarly books focusing on global franchising including:

1. The Economics of Franchising, Roger D. Blair, Francine Lafontaine (2005)
2. Incentive Based Franchise- a New Model for World Governance, Sondlo L. Mhlaba (2005)

Increased interest in the global context of franchising is evident in the emergent literature on the subject. This book adds to the scant but growing academic literature on franchising globally by examining theoretical and practical aspects of franchising from the standpoints of franchisors and policy makers. The book is divided into four sections. Section I deals with franchising development explaining why franchisors use franchising, the social and economic benefits and costs of franchising to host markets, and measuring the economic impact of franchising on a locality. Section II focuses on financial impact of franchising to franchisors, how franchisors evaluate foreign markets, master international franchising, and how franchisors cluster. Section III evaluates franchising conditions in three emerging markets: Russia, the Philippines, and Slovenia. Finally, section IV examines two cases of companies using franchising internationally, one of Kodak in China and the other of Marks and Spensor internationally. A chapter by chapter review in each section follows.

**SECTION I: FRANCHISING DEVELOPMENT**

Chapter 2 examines when franchisors use franchising. The question of whether to franchise or to own has garnered research interest in recent years. Two popular approaches used to explain the proportion of franchising in the franchisor’s system, resource-scarcity and agency theories, are explained and tested for the retailing sector. The chapter claims that a complete explanation of franchising needs both. The study combines both theories to explain the proportion of franchised outlets in the US retailing sector and tracks the statistics associated with this industry for seven years in the 1990s. The findings show mixed results with regard to previous studies and hypothesized relationships. It shows that the proportion of franchising used by retailers is positively related to size (number of outlets) and geographical scope, and negatively related to the rate of growth and the level of investment. Age and royalty rates are not found to be significant to the proportion of franchising. More sizable franchisors with greater scope of operation, and those with lower level of system growth and required level of investment, are more likely to use franchising in their future expansion.

Chapter 3 analyzes the economic and social impacts of international franchising on regional development from the perspective of the host market with emphasis on developing countries. The conventional wisdom that prevails in the West is that franchising provides a net benefit to the host
market. In addition to the obvious economic benefits of employment, output and tax, franchising development contributes qualitatively by injecting expertise and training in various industries and increasing the entrepreneurial and managerial capabilities and skills of the labor force. On the other hand, the unique nature of international franchising creates some social pressures, such as a potential increase in a cultural clash and a perceived reduction in national culture. The chapter discusses the implications of franchising to the developing counties, assessing both the potential benefits and their associated costs. Using the framework of this chapter, researchers, policy makers, and franchising practitioners can better evaluate the total impact of franchising and its desirability in the less affluent world.

Chapter 4 seeks to understand the potential economic impact of franchising on a local economy. Using Economic Analysis in Planning (IMPLAN) model, the study measures the economic effects of spending in three service industries in which franchising prevails: (1) eating and drinking, (2) management consulting, and (3) hotel sectors. IMPLAN is an economic analysis system designed to measure the direct, indirect and induced effects of industry spending on economic output and employment, allowing planners to assess the industry-specific differences. This article examines the economic impacts of potential franchising investment in a small city in Upstate New York. The total economic output multipliers found were about 1.14 and varied little in the three sectors. In contrast, there were considerable variations in the employment multiplier. Eating and drinking places, with 38 jobs created for every million dollars spent in the local economy, had the highest employment multipliers among the three industries.

SECTION II: FRANCHISING STRATEGIES AND TYPES

Chapter 5 sheds light on the debate on franchising success/failure. This debate has developed among franchising practitioners, franchising researchers, and support groups relating to the promise of the franchising as an organizational form and a method of distribution. On the one hand, some espouse franchising as a strategy for growth that limits the risk of failure. This group is typified by franchisors, franchise associations, and selected industry observers. On the other hand, another group of researchers has departed from accepted notions of the franchising success, claiming that it is no less risky than other forms of business. Given the apparent disagreement between the two groups, the purpose of this chapter is to investigate the relationship between the use of franchising at the chain level and one measure of the chain's financial performance, return on equity (ROE), in the context of the DuPont model. The results show no appreciable difference in the financial performance of franchising vs. non-franchising firms in the
restaurant sector among publicly-traded firms. Therefore, franchising form neither improves nor worsens the return on equity for brands in the restaurant sector.

Chapter 6 provides a prescriptive framework for analyzing the foreign environments of franchising for international expansion, mostly from an American perspective. The chapter develops a macro environmental model of international franchising that delineates the critical socio-economic country factors associated with the expansion of US international franchising. These factors divided into (1) economic, (2) demographic, (3) distance, and (4) political dimensions, and should be useful to both franchisors wishing to expand to foreign markets and academicians wanting to build empirical models explaining the internationalization of US franchising systems. In a related study, using correlation analysis to link environmental factors with international franchising activity, Alon, Toncar and McKee (2000) found that per capita GDP, level of population, urbanization, female labor-force participation, level of individualism, and sex role differentiation are positively related to international franchising, while political risk and, to a lesser extent, power distance and uncertainty avoidance, are negatively related to international franchising.

Chapter 7 investigates a common form of international franchising expansion, master international franchising. Master international franchising is the fastest growing and most prevalent mode of entry by U.S. based franchisors abroad. The purpose of the chapter is to develop propositions concerning the impact of select organizational variables on the use of master franchising agreements by business-format franchisors overseas. The article proposes that the organizational factors of master international franchising divide into resource-based, knowledge-based, and strategy-based explanations. Franchisors with modest resources, internationally unknown brand names, little experience in international markets, and know-how that is transferable are more likely to use master franchising as an international franchising mode of entry. These franchisors will also tend to charge more of the price upfront through the franchisee fee and less over time through royalties and to pursue a multi-domestic strategy.

Drawing upon Castrogiovanni & Justis’ (1998) organizational configurations of franchising firms and the literature on master franchising, chapter 8 looks at how internationally-minded franchisor group together. The chapter empirically examines the typologies of internationally-minded franchisors at the system level and the mode of entry they are likely to use when expanding overseas. Applying cluster analysis to a sample of 261 US-based franchisors, we found evidence of three types of franchisors, corresponding to Castrogiovanni and Justis’ *entrepreneurial, confederation,* and *carbon-copy* forms. We also found that master international franchising was the preferred expansion mode for the *confederation* form of franchisors,
followed by carbon-copy and entrepreneurial franchisors. This research extends the study of franchise configurations to internationally-bound franchisors. The findings support the view that franchise groupings exist and that the characteristics of each may help explain variance in franchising strategies.

SECTION III: FRANCHISING IN EMERGING MARKETS

Section III presents contemporary reviews of franchising conditions of three emerging markets: Russia, Philippines, and Slovenia. Emerging markets embody the most dynamic opportunities for global franchisors (Welsh and Alon, 2001; Alon and Welsh 2001). Chapter 9 makes a contribution to the state of knowledge on franchising in Russia by analyzing Russia as a target market for international franchising entrepreneurship. First, past research and literature on franchising in Russia and other emerging markets is reviewed. The country's franchising environment is examined in relation to five environmental factors: (1) demographics, (2) economy, (3) social and political environment, (4) culture, and (5) legislation. Some preliminary information on a major franchising system in Russia is presented. A complete SWOT (strengths, weaknesses, opportunities, and threats) analysis for international franchising in Russia is provided in the conclusion section.

Chapter 10 analyzes the franchising environment in the Philippines, an emerging market in Southeast Asia with close and long historical ties to the US market. As part of the exploration of the potential challenges and opportunities in the Philippine market, the authors peruse the environmental factors franchising from political, legal, economic, financial and social standpoints, the competitiveness in the franchising sector, the four marketing P’s, strategic control measures, and the modes of entry available to prospective market entrants. The research information and strategies provided is beneficial to academics and business people seeking to understand the franchising dynamics in a key emerging market in Southeast Asia. It provides the background needed for the creation of a country-specific international market entry plan for potential franchisors and franchisees wishing to operate in the Philippines.

Chapter 11 proposes that research of franchising in the EU requires a heuristic examination of operative networks in order to establish the existence of key parameters of franchising as contained in the European Franchise Federation’s definition of franchising. The chapter discusses the conditions for franchising development in the Central European context of Slovenia. If many studies of franchising consider top-down approaches in replication of successful business formulae, this is a case of gradual
development of a franchise network as it develops out of a voluntary chain. Transitional conditions may negatively influence the growth and the long-term well being of a franchise system, coupled with the change in the span of autonomy required for conversion of a voluntary chain into a franchise system.

SECTION IV: CASES IN INTERNATIONAL FRANCHISING

Section IV present two cases of companies utilizing franchising in their international operations: Kodak, an American imaging firm, and Marks & Spencer, a British retailer. What is interesting about these firms is that both do not utilize franchising in their domestic market, but do franchise abroad. The conditions under which these companies chose to use franchising are discussed in the context of these firms’ internationalization strategies.

The first case in this section, presented in Chapter 12, is focused on Kodak’s franchising in China, the largest emerging market in the world. According to Kodak, China poses unparalleled opportunities for low-cost production in addition to opportunities to market products and services to the world’s largest nation. According to the company’s estimate, China will become the largest market in the world for photographic products and services within the next 10 years. The chapter reviews Kodak’s operations in China and presents an interview with a local franchising manager in Shanghai, the largest and most dynamic city in China. It provides a unique glimpse into the inner working of the organization’s franchising activities in China.

In contrast to chapter 12 which examines franchising arrangement in China for an American multinational company, chapter 13’s case study describes the internationalization of Marks & Spencer (M&S), a giant British retailer, which in part involved the usage of franchising. In the late 1990s, the company suffered a series of misfortunes, both at home (Britain) and abroad. The case reviews the different modes of entry the company used in selected regions and markets. The company made large investments in Europe and North America. Franchising was primarily used in emerging markets.
REFERENCES


Chapter 2
Why Do Companies Use Franchising?

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INTRODUCTION

Franchising has experienced unprecedented growth during the last two decades both in the United States and abroad (Alon and McKee 1999). In the United State of America, for example, according to the US Department of Commerce, the number of business format franchises increased almost tenfold between 1972 to 1988 (Kostecka 1988). While in 1992 franchise sales accounted for $803 billion in sales, the International Franchising Association (1995) predicted that franchise sales will reach $1 trillion by the year 2000. In 2004, the International Franchising Association reported that franchising accounts for 760,000 businesses generating $1.53 trillion, about 10% of the private sector economy.

The study on the use of franchising is relevant to small business across multiple industries. According to the Uniform Franchise Offering Circular (UFOC), there were 1,178 franchisors with over 320,000 outlets, representing over 18 different sectors, operating in the United States in 1997. Twelve percent had no franchisee-owned units, 16 percent had less than 10 outlets, and 27 percent had between 11-50 units. Those with the largest number of units (500 and above) made up only nine percent, the smallest concentration of franchised systems (International Franchise Association 1999). In this chapter’s sample of retail franchises, about a third of the franchisors had less than 10 franchisees, while 10 percent had no franchisees at all in their system. The median age and size were 11 years and 30 outlets, respectively. Therefore, this chapter is especially relevant to small business management, particularly from the franchisor’s standpoint.

This chapter uses two popular approaches, resource-scarcity and agency theories, to examine the proportion of franchising in the US retailing sector. Although there is some disagreement between resource-scarcity and agency theorists regarding the causal factors of domestic franchising, by integrating variables from both the agency and resource-scarcity theories researchers have developed models with greater explanatory power (Carney and Gedajlovic 1991; Combs and Castrogiovanni 1994).
Using previously established theories and variables, this research innovates by examining franchising over time (longitudinally), rather than at a point in time (cross-sectionally), and by focusing on one industry, namely retailing. Examining one industry over time allows the researcher to (1) obtain an in-depth understanding of the industry, (2) control for competitive and industry variations, and (3) increase the sample size associated with the studied industry. Dant and his co-authors (1996) proposed that industry aggregation may hide industry differentials and margins, masking the true nature of the causal factors between organizational variables and the proportion of franchising. Resource and agency variables may also impact the relative proportion of franchising depending on the industry studied. Indeed, the meta-analysis conducted by Dant and others in 1996 found that industry-specific differences were such that analyses that did not take them into account could have flaws in their conclusions. Furthermore, comparing franchising across industries elides the obvious facts that different industries have different motivations for franchise-based expansion and that there will be variations in the degree to which individual industries will tend to franchise.

In the conclusion of their meta-analysis, Dant and his colleagues (1996, p. 440) wrote that “as for future research, foremost, there is an urgent need to study ownership redirection in sectors other than restaurants.” Our focus is on the retailing industry because (1) franchising has been associated with the retailing sector (Cross and Walker 1987); (2) much of retailing is franchised, accounting for $900 million in sales and 40 percent of aggregate retail sales in the US (Rubel 1995); and (3) franchising is expected to grow in importance for the retailing industry. Therefore, this chapter seeks here to expand Dant’s suggestion that a focus upon one industry is appropriate, and moves from the perhaps stale ground of restaurant franchising into a focused analysis of the retail industry from a business-format franchising perspective (defined below), with appropriate sidelong glances at out-of-industry examples that illustrate our points.

DEFINITIONS OF FRANCHISING

Franchising divides into product/trade-name franchising and business-format franchising. “Product/trade-name franchising is a distribution system in which suppliers make contracts with dealers to buy or sell products or product lines” (Falbe and Dandridge 1992, p. 43). The International Franchise Association (IFA), the major business-format franchising trade association, defines franchising as “a continuing relationship in which the franchisor provides a licensed privilege to do business, plus assistance in organizing, training, merchandising and management, in return for a consideration from the franchisee” (Franchise Opportunities Handbook
1994, p. ix). Similarly, the US Department of Commerce defines franchising as "an ongoing business relationship between franchisor and franchisee that includes not only product, service and trade-mark, but the entire business concept itself—a marketing strategy and plan, operating manuals and standards, quality control, and continuing process of assistance and guidance" (Kostecka 1988, p. 3).

The difference between product/trade-name franchising and business-format franchising is that the latter offers a method of operation or business system that includes a strategic plan for growth and ongoing guidance (Falbe and Dandridge 1992). Because business-format (from hence forth franchising) franchising is the basis for most franchising ventures, it is the focus of this chapter.

THEORETICAL ANTECEDENTS

The focus of resource-scarcity and agency theories is different, requiring different causal connections for their respective explanations of franchising. Resource-scarcity theories attempt to explain franchising as the desire to expand with scant resources, while agency theories postulate that firms franchise to minimize monitoring and shirking costs. Traditional measures of resources include size, age and rate of growth (Combs and Castrogiovanni 1994). According to resource-scarcity theorists, the more resources a firm has, the less it needs franchising to expand and, therefore, a negative relation is hypothesized between size, age, rate of growth and the proportion of franchising. Geographical scope of operation, investment and royalty hypotheses have all developed out of agency theory. To minimize the amount of monitoring needed, geographically dispersed units have a greater tendency to be franchised. As a further guarantor of investment and to maximize profits, companies will often demand higher initial investments from franchisees and will require large royalties to capture the value of intangibles such as brand-name, trade-mark and know-how (Combs and Castrogiovanni 1994). Table 2.1 shows the hypotheses derived from these competing theories. The section that follows provides a review.

Table 2.1: The Hypotheses, Variables, and Measurements

<table>
<thead>
<tr>
<th>Hypothesis</th>
<th>Variable</th>
<th>Measurement</th>
<th>Relationship</th>
</tr>
</thead>
<tbody>
<tr>
<td>H1</td>
<td>LSize</td>
<td>Log (total # of units)</td>
<td>Negative</td>
</tr>
<tr>
<td>H2</td>
<td>LAge</td>
<td>Log (years in operation)</td>
<td>Negative</td>
</tr>
<tr>
<td>H3</td>
<td>Growth</td>
<td>Yearly growth rate</td>
<td>Positive</td>
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<td>H4</td>
<td>Scope</td>
<td>0=Local 1=National</td>
<td>Positive</td>
</tr>
<tr>
<td>H5</td>
<td>Investment</td>
<td>Mean start-up costs</td>
<td>Positive</td>
</tr>
<tr>
<td>H6</td>
<td>Royalties</td>
<td>Mean royalties</td>
<td>Positive</td>
</tr>
</tbody>
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