FRANCHISING: HYBRID ORGANISATIONAL ARRANGEMENT FOR FIRM GROWTH AND NATIONAL DEVELOPMENT

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Abstract
This paper examines the practice of franchising as a strategy by which entrepreneurs can expand their venture and make substantial return from their investments. The paper tries to explore the extent to which franchising is being practiced in Nigeria and the resultant effect of franchising on the national economy. The study was done by taking intensive study of Nigerian business world to see the extent of the practice of franchising system of business. The result of this study shows that franchising is not well known or practiced in Nigeria. Only a handful of business entities such as the Nigerian Bottling Company and some fast food companies have been engaged in franchising. The paper recommends that government should create a greater awareness of the franchise strategy so that more investors will be aware of it and invest in it. This will create more employment opportunities, reduce poverty level, and ultimately improve the Gross Domestic Product of the nation.

Key words: *Entrepreneurship, Franchising, Market, National Development.*

Introduction

A number of strategies are available to the entrepreneur for the expansion of his venture. However, one of these strategies that are mostly ignored by entrepreneurs in new venture expansion is franchising. This paper examines the practice of franchising as a hybrid organizational arrangement by which entrepreneurs can expand their business. This paper is important because proper knowledge and application of franchising business is imperative for firm growth and national development. The author conducted an intensive study of Nigerian business world and discovered that franchising, unlike what obtained in developing countries such as the United States of America where, one out of every three dollars spent by Americans for goods and services is spent in a franchise business. This cannot be said of Nigeria. This is because many entrepreneurs in this part of the world are yet to know the benefits inherent in franchising (Ike-Okoh, 2006).

In this study, we explore what franchising is; we also consider the scope of franchising and examine the criteria for determining a franchise's stature from the perspective of both the franchisee and franchisor. We also look at franchise relationship model. We conclude by examining the current trend of thinking on franchising and how Nigeria business can profit from it.

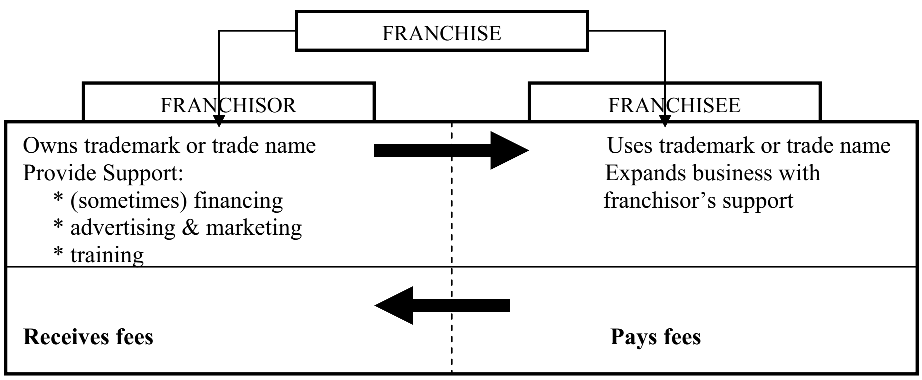
Literature review
Concept of Franchising

Historically, the word franchise is of French origin. It simply means "privilege" or "freedom". Hisrich, Peters and Shepherd (2005) see franchising as a means of new entry that can reduce the risk of downside loss for the franchise. They see franchising as an alternative means by which an entrepreneur may expand his business by having others pay for the use of the name, process, product, services and trademark. It can be used as a growth mechanism by the organization (i.e. the franchisor). It is sharing an entrepreneurial vision and working together to make it a reality. According to Otokiti (2004) franchising is a business arrangement in which the franchisor grants the franchisee the right to do business in a prescribed manner over a certain period of time in a specified way. However, franchising can be used to describe business format in which the franchisor offers a complete business package. Thus, Beshel (2001) says a franchise is the agreement or license between two legally independent parties which gives:

- A person or group of people (franchisee) the right to market a product or service using the trademark or trade name of another business (franchisor).
- The franchisee the right to market a product or service using the operating methods of the franchisor.
- The franchisee the obligation to pay the franchisor fees for these rights.
- The franchisor the obligation to provide rights and support to franchisees.

A simple franchise agreement is illustrated in figure 1 below:

Figure 1: A simple franchise agreement



Source: Adapted from Beshel (2001)

It is pellucid from the above figure that both the franchisor and franchisee have rights and obligations to each other.

In order to distinguish it from other forms of agreement, the following important features characterized franchise.

A Contract; a franchise is based on a contract between the franchisor and the franchisee. The contract tells each party what each is supposed to do.

A Purpose; the franchisor and the franchisee agree that their purpose is to provide for efficient distribution of the goods or services.

Resources; the franchisee usually contributes money and agrees to manage the local franchise business to the best of his ability for monetary gain. The franchisor contributes other resources such as business idea, trademark, training, technical know-how, legal framework and advise.

A business entity; there is a separate legal entity. The franchise outlet is set up as a separate business with a distinct identity, different from the franchisee's existing business,

A common public identity; both parties support a common public identity through the use of a common trade name, trademark, architectural design, advertising, and product brand.
A financial arrangement: the franchisee is expected to make a profit from the venture and compensate the franchisor with a franchising fee and royalties as the case may be.

Theoretical Framework of Franchising

The success of the franchisor depends on the success of franchisee. Therefore the franchisor's attempt to select franchisees that will work hard and take the responsibility for their outlets, yet be willing to listen to advise and cooperate (Otokiti, 2004).

Hisrich et al. (2005) argued that not all franchise is right for every entrepreneur. An entrepreneur must evaluate the franchise alternatives to decide which one is most appropriate. Following are the number of factors that should be assessed before making final decision.

- The unproven versus the proven franchise.
- Financial stability of franchise.
- Potential markets for the new franchise.
- The profit potential for a new franchise.

They also argued that entrepreneurs face certain problems in starting up a new venture in areas such as; product acceptance, management expertise, meeting capital requirements, knowledge of the market, and operating and structural controls, but that in franchising, the risks associated with each are minimized through the franchise relationship.

Types of Franchises

There are two main types of franchises: product distribution franchises and business format franchises.
Product Distribution Franchises: According to Beshel (2001) product distribution franchises simply sell the franchisor's product and are supplier-dealer relationships. In product distribution franchising, the franchisor licenses its trademark and logo to the franchisees but typically does not provide them with an entire system for running their business. This type of franchise is commonly found in soft drink distributors, automobile dealers and filling stations.

Although product distribution franchising represents the largest percentage of total retail sales, most franchises available today are business format opportunities.

Business Format Franchise: Stokes (1998) argued that the word franchising is more commonly used to describe business format franchising. This, he said, is seen as a more in-depth relationship between franchisor and franchisee than the simple product distribution or trademark licensing agreement. Business format franchises, says Beshel (2001) not only use a franchisor's product, service and trademark, but also the complete method to conduct the business itself, such as the marketing plan and operations manuals.

Business format franchising represents a complete package that allows the franchisee to use the format proven by the franchisor, whilst retaining independence as a business. There is an agreement between the two parties that sets out how the business will be run and the obligations of both parties. It is an organizational form based on a legal agreement between a parent organization (the franchisor) and a local outlet (the franchisee), to sell a product or service using the brand name developed and owned by the franchisor. The franchisor typically sells the franchisee a right to use this intellectual property in return for a lump sum payment and an annual royalty fee based on sales for a specified period of time (Miller and Grossman, 1990).

In addition, the franchisee usually agrees to adhere to franchisor requirements for product mix, operating procedures and site selection (Robin, 1978).

Business format franchising is a popular example of a hybrid organizational format that incorporates elements of both markets and hierarchies (Williamson, 1991). It is a hybrid alternative since the franchisor both retains a degree of ownership and authority over the use of the trade name, operating procedures and the location of outlets and contracts with independent entrepreneurs to operate the units (Child, 1987).

Business format franchising provides a useful laboratory for examining the effect of hybrid organizational forms of the rate of growth. Franchisors exploit the same retail markets using the same business concepts through both franchised and company owned outlets. Consequently, by looking at franchisors, researchers can examine the effects of organizational format on the rate of the growth of firms holding constant, firm and markets differences (Shane, 1996).

Early forms of franchising were linked to the classic argument that economic organizations follow two general forms, viz: markets and firms (Coase, 1937). Theorists identified franchising as a hybrid manifestation of the two forms because it has both market-like and firm-like qualities (Norton, 1988; Brickley and Dark, 1987, Matthewson and Winter, 1985). Franchising is seen as a means of obtaining scarce capital, as the franchisee is generally required to make a substantial investment on the business.

Franchisees share risk with the franchisor. Franchising is also identified as a way of addressing the agency problem, specifically, the issue of monitoring managers (Brickly and Dark, 1987; Matthewson and Winter, 1985). Franchisees with substantial investments are more motivated to minimize revenues through administrative efficiency and protection of the franchise brand, while minimizing operational costs (Welsh, Alon and Falbe, 2006). The issues of monitoring and risking are greatly increased in international franchising by both geographical and cultural distance (Fladmoe-Lindquist and Jacque, 1995).

Types of Franchise Arrangement

Because so many franchisors, industries and range of investments are possible, there are different types of franchise arrangements available to a business owner. Two types of franchising arrangements are: single-unit franchise and multi-unit franchise.

A Single-unit Franchise is an arrangement where the franchisor grants a franchisee the rights to open and operate only one franchise unit. This is the simplest and most common type of franchise. It is, however, for a franchisee to purchase additional single-unit franchises once the original franchise unit begins to prosper. This is then considered a multiple, single-unit relationship (Beshel, 2001).

A Multi-unit Franchise is an agreement where the franchisor grants a franchisee the rights to open and operate more than one unit. A multi-unit franchise can be achieved in two ways, namely: an area development franchise or a master franchise.

Under an **area development franchise,** a franchisee has the right to open more than one unit during a specific time, within a specified area for instance; a franchisee may agree to open 3 units over a three-year period in a specified territory.

A master franchise agreement gives the franchisee more rights than an area development agreement. Apart from having the right and obligation to open and operate a certain number of units in a defined area, the master franchisee also has the right to sell franchises to other people within the territory. This is known as sub-franchises. Therefore, the master franchisee takes over many of the tasks, duties and benefits of the franchisor, like providing support and training, as well as receiving fees and royalties.

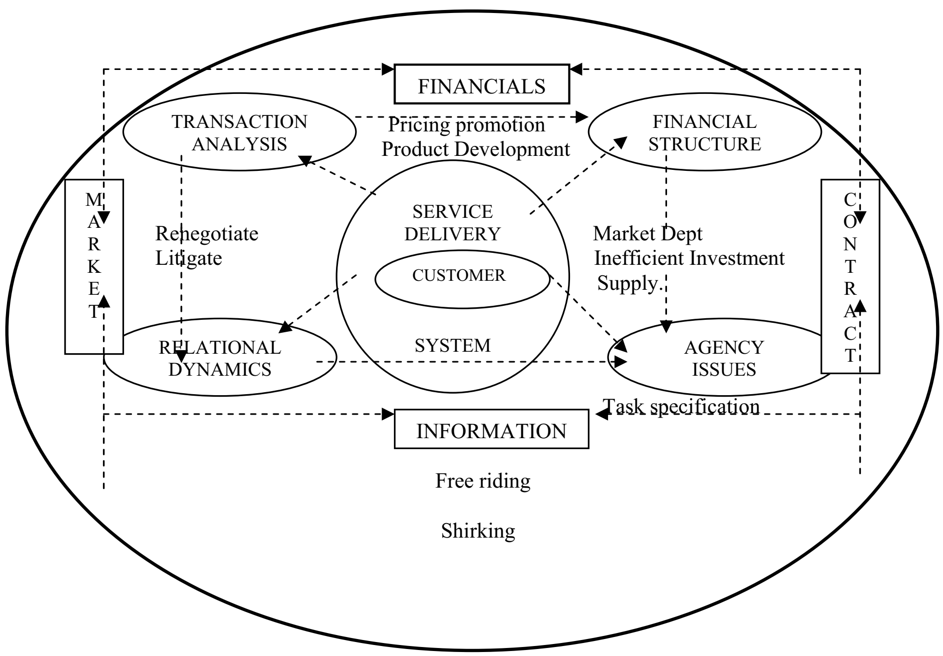
Franchise Relationship Model

The Franchise Relationship Model (FRM) illustrates how a franchisor can most efficiently construct a franchising company and how a franchisee can determine which company to join. The FRM also helps to distinguish between the tasks that need to be carried out under a corporate umbrella and those to be executed by the individual franchisee. Besides, the FRM is a tool that can be used to judge the efficiency of success potential of a franchise opportunity by both the franchisor and franchisee.

The FRM is a series of franchise principles, each of which when joint together form an interlocking business concept that fixed itself when the linkages are implemented efficiently. The process begins in the centre with the customer and moves to the service delivery system. The other major areas of concern are transaction analysis, financial structure, agency issues, and relational dynamics.

Transaction analysis considers which transactions are better served by the franchiser at a national level and which, at the local level by the franchisee (Williamson, 1991). The financial structure flows from profoma analysis of customer demand and the cost associated with development and execution of the service delivery system. Agency issues concern delegating responsibility to a partner (Lafon-taine, 1992). Relational dynamics is the area that allows the partnership between franchisor and franchisee to continually grow and develop as the business continues to expand (Mcneil, 1980).

Figure 2: Franchise Relationship Model



Source: Adapted From Timmons and Spinelli, (2004) The FRM in figure 2 above illustrates how a franchisor can construct a franchising company and the pathway for implementing it in the most entrepreneurial way.

Current Trends Of Thinking On Franchising

According to Welsh et al. (2006) new symbiotic relationships are created when retail franchising expands into developing countries. Retail franchising allows firms to achieve the expanded reach and efficiencies associated with internationalization more rapidly and effectively than the firms could accomplish on their own. Etemad, Wright and Dana (2001) developed a paradigm called the Interdependence Paradigm to explain these franchise-marketing networks. They said that franchising involves a network of franchisees under the guidance of a parent firm, the franchisor. Franchisors that are well established can achieve greater efficiency by incorporating smaller franchisees from the emerging markets into international franchise networks. It was also pointed out that franchising could help local ownership requirements in regulated sectors. Therefore, franchising enhances the competitiveness of franchisors, while contributing to the development of emerging markets. The symbiotic interdependence that forms between franchisor and franchisees in a network, which is viewed as a paradigm shift from independence to interdependence, have far reaching consequences and have a major impact on the way business is handled internationally.

Franchising in emerging markets also offers the host countries certain advantages. These benefits include obtaining foreign currency with little capital outlay, increases in employment and thereby growth in the franchisor's tax base and gross domestic output. Franchise growth and development spawn entrepreneurial development comprised of small and medium enterprise networks.

Retail franchising may have adverse effects on the host market. It can sometimes supplant traditional and local elements, which over time can lead to homogenization and westernization of preferences, especially among the youth. International retail franchising often times has the effect of displacing local industry. Alon (2004) examined the macro-environmental impacts of franchising on the host and home markets and included in his analysis economic, political and social ramifications. He concluded that the probable overall impact however, is positive in the long.

Governments, according to Welsh et al. (1006) have increasingly become aware of the benefits that franchising has to offer to their country. As a result, many governments are in the process of improving their country's business environment to attract high quality franchises. These improvements have included positive legislation for franchise regulations, trade associations, establishing support organizations, and franchise education programmes.

In recent years, franchisors have built huge portfolios of brand and grouping them to take advantage of retail space. Franchisees too, are learning this approach seeking to spread their costs over a larger business. Those in the business of franchising in Nigeria today are projecting that the franchising market in Nigeria will grow at 10 per cent annually by 2010. This is premised on the level of awareness on the concepts and best practices on franchising, which is presently low (Ike-Okoh, 2006).

Experts, according to Ike-Okah, (2006), say the business format franchise is less exposed to the problem associated with conventional business such as recruiting and retraining staff and the security of stock and cash. That is, it is a system that makes it easier for companies to expand internationally and some franchise companies are among the largest multinational corporations in the world. A good example is the Coca-Cola Company that operates a franchise through the Nigerian Bottling Company (NBC). Today, NBC is one of the biggest companies operating in Nigeria.

Conclusion

The scope of franchise concept can be local, regional, national, or international (Timmons and Spinelli, 2004). Recent trends in the business environment have brought about innovative ways in which firms can take the lead in their industry even in the face of great competitors. This is because entrepreneurs that are using franchising as business strategy are making big profits and are gaining even stronger brand names through it. By maintaining the same standards operated in the parent company, franchisees stand a great chance of maintaining their customers' loyalties.

For franchising business to gain great ground and popularity in Nigeria and be very good investment for up and coming entrepreneurs, the following recommendations need to be followed.

First, the franchisors should make it easier for aspiring franchisees to come in by not making their royalty fees too large that interested investors would be discouraged to invest.

Second, the government should provide entrepreneurs with subsidized grants that would make it easy for them to buy into a franchise system, grow their franchise business, pay back loans and still be profitable.

Third, franchisors and franchises should not focus only on just maximizing profits, but should take into consideration customer care and be given them quality products and service.

Finally, the government should create a greater awareness of the franchise strategy so that more investors will be aware and invest in it. This will create more employment opportunities, reduce poverty level and improving the gross domestic product of the nation.

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