CHAPTER III

THEORITICAL FRAMEWORK

3.1 Franchising Theoritical Framework

3.1.1 Reason for Franchising

The franchising is defined in many ways. In this study, we use a broad definition to encompass its wide diversity. Franchising is a marketing system revolving around a two-party legal agreement whereby one party (the franchisee) is granted the privilege to conduct business as an individual owner but is required to operate according to methods and terms specified by the other party (the franchisor). The legal agreement is known as the franchise contract, and the privileges it contains are called the franchise. The International Franchise Association describes the definition of franchise as follows:

"A franchise operation is a contractual relationship between the franchisor and franchisee in which the franchisor offers or is obliged to maintain a continuing interest in the business of the franchisor in such areas as know-how and training; where in the franchisee operates under a common trade name, format op procedure owned by or procedure owned by or controlled by the franchisor, and in which the franchisee has or will make a substantial capital investment in his business from his own resources."

These definitions have in common the following features;

(1) A franchise involves a contractual relationship between the parties under which one party (the franchisor) license the other party (the franchisee) to carry on business under a name, etc owned or associated with the franchisor.

(2) Control by the franchisor over the way in which the franchisee carries on that business.

(3) Provision of assistance to the franchisee by the franchisor in running the business.

(4) The businesses are however separate; the franchisee provides and risks his own capital.[1]

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[1] John Adams, K.V.Prichard Jones; Franchising;; second edition Butterworth&Co (Publishers) Ltd; 1987; page 9

Over the last two decades, franchising has emerged as a popular expansion strategy for a variety of product and service companies, especially for smaller business that cannot afford to finance internal growth. Recent Department of Commerce statistic demonstrates that retail sales from franchised outlets comprise nearly 40percent of all retail sales in the United States, estimate at over $640billion and employing some 7.3million people in 1988. Notwithstanding these impressive figures, franchising as a method of marketing and distributing products and services is really only appropriate for certain kinds of companies. Despite the favorable media attention the franchising has received over the past few years as a method of business growth, it is not for everyone. There is a host legal and business prerequisites that must be satisfied before any company can seriously consider franchising as an alternative for rapid expansion. Many companies prematurely select franchising as a growth alternative and then haphazardly assemble and launch the program. Other companies are urged to franchise by unqualified consultants or advisors who may be more interested in professional fees that in the long-term success of the franchising program. This has caused finance distress and failure at both the franchisor and franchisee level and usually results in litigation. Current and future members of the franchising community must be urged to take a responsible view toward the creation and development of their franchising system.

There are wide variety of reasons cited by successful franchisors as to why franchising has been selected as a method of growth and distribution. Through franchising, they are able to:

- Obtain operation efficiencies and economies of scale
- Achieve more rapid market penetration at a lower capital cost
- Reach the targeted consumer more effectively through cooperative advertising and promotion
- Sell products and services to a dedicated distributor network
- Replace the need for internal personnel with motivated owner/operators
- Shift the primary responsibility for site selection, employee training and personnel management, local advertising, and other administrative concerns to the franchisee, licensee, or joint venture partner with the guidance or assistance of the franchisor

In the typical franchising relationship, the franchisee shares the risk of expansion market share of the franchisor by committ ng its capital and resources to the development of satellite locations model after the proprietary business format of the franchisors. The risk of business failure of the franchisor is further reduced by the improvement in competitive position, reduced vulnerability to cyclical fluctuations, the existence of a capital market for the franchisor's proprietary products and services (due to network of franchisees), and the reduced administrative and overhead costs enjoyed by a franchisor.

Responsible franchising is the only way that franchisors and franchisees will be able to harmoniously co-exist in the twenty-first century. Responsible franchising requires a secure foundation from which the franchising program is launched. Any company considering franchising as a method growth and distribution or any individual considering franchising as a method of getting into business must understand the key components of this foundation[1]:

(1) A proven prototype location (or chain of stores) that will serve as a basis for the franchising program. The store and stores must have been tested, refined, and operated successfully and be consistently profitable. The success of the prototype should not be too dependent on the physical presence or specific expertise of the founder of the system.

(2) A strong management team made up of internal officers and directors who understand both the particular industry in which the company operates and the legal and business aspects of franchising as a method of expansion.

(3) Sufficient capitalization to launch and sustain the franchising program to ensure that capital is available for the franchisor to provide both initial as well as ongoing support and assistance to franchisees (a lack of well written business plan and adequate capital structure is often the principal cause of demise of many franchisee).

(4) A distinctive and protected trade identity that includes federal and state registered trademarks as well as a uniform trade appearance, signage, slogans, trade dress, and overall image.

(5) Proprietary and proven methods of operation and management that can be reduces to writing in a comprehensive operations manual, not too easily duplicated by competitors, maintain their value to the franchisees over an extended period of time, and be enforced through clearly drafted and objective quality control standards.

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[1]Franchising & Licensing Two ways to build your business; Andrew J. Sherman; American Management Association

(6) Comprehensive training program for franchisees both at the company's headquarters and on-site at the franchisee's proposed location at the outset of the relationship and on an ongoing basis.

(7) Field support staff who are skilled trainers and communicators and must be available to visit and periodically assist franchisees as well as monitor quality control standards.

(8) A set of comprehensive legal documents that reflect the company's business strategies and operating policies. Offering documents must be prepared in accordance with applicable federal and state disclosure laws, and franchise agreements should strike a delicate balance between the rights and obligations of franchisor and franchisee.

(9) A demonstrated market demand for the product and services developed by the franchisor, which will be distributed through the franchisees. The franchisor's products and services should meet certain minimum quality standards, not be subject to rapid shifts in consumer preference and be proprietary in nature. Market research and analysis should be sensitive to trends in the economy and specific industry, the plans of direct and indirect competitors, and shifts in consumer preferences.

(10)A set of carefully developed uniform site selection criteria and architectural standards that can be readily and affordably secured in today's competitive real estate market.

(11)A genuine understanding of the competition (both direct and indirect) that the franchisor will face in marketing and selling franchises to prospective franchises as well as the competition the franchisee will face when marketing products and services

(12)Relationship with suppliers, lenders, real estate developers, and related key resources as part of the operations manual and system.

(13)A franchisee profile and screening system in order to identify the minimum financial qualifications, business acumen, and understanding of the industry that will be required by a successful franchisee.

(14)An effective system of reporting and record keeping to maintain the performance of the franchisees and ensure that royalties are reported accurately and paid promptly.

(15)Research and development capabilities for the introduction of new products and services on an ongoing basis to consumers through the franchised network.

*(16)*A communication system that facilitates a continuing and open dialogue with the franchisees and as a result reduces the chance for conflict and litigation within the franchise network.

*(17)*National, regional, and local advertising, marketing, and public relations programs designed to recruit prospective franchisees as well as consumers to the sites operated by franchisees.

3.1.2 Prerequisites to Launch a Franchise Program

The most important strategic prerequisite for the success of any business format franchise system is the operation and management of a successful prototype. This prototype location is where all operating problems must be resolved, recipes and new products tested, equipment and design decisions made, management and marketing techniques tested, a trade identity and goodwill established, and financial viability proven. It is not enough to have a prototype unit that is "some what similar" to the system and format that will be franchised. The franchisor's location must be exactly replica of the prototype. In short, the franchisor is selling a tried and tested package to a franchisee, and the contents of that package must be clearly identified prior to sale.

The concept of a system or prescribed business format that is operated according to a uniform and consistent trade identity and image are at the heart of a successful franchising program. Therefore, a prospective franchisor must be able to reduce all aspects of running the business to be franchisees in the day-to-day operation of their business. These systems must be adequately and clearly communicated in the initial and ongoing training program. If a company offers services that are highly personalized or a product that is difficult to reproduce, then franchising may not be the most viable alternative for growth because of the difficulty in replicating these systems or products in the operator's manual or in the training program. Similarly, if all the "kinks" in the system have not yet been worked out, it is probably premature to consider franchising.

There are a number of other important business and strategic factors that must be considered before franchising. First, franchising should not be viewed as a solution to undercapitalization or as a get rich quick scheme. While it is true that franchising is less capital-intensive than is construction of additional company-owned sites, the initial start-up costs for legal, accounting, and consulting fees can be extensive. Second, franchisors must view franchising as the establishment of a series of long-term relationships, and the ongoing success of the company as a franchisor will depend on the harmony of these relationships. A field support staff must be built to provide ongoing services to the existing franchisees, as well as to maintain quality control and uniformity throughout the system. New products and services must be developed so that the franchisee can continue to compete with others in its local market. Innovative sales and marketing strategies must be continually developed to attract new customers and retain existing patrons of the franchised outlet. If the franchisor expects the franchisee to continue to make its royalty payment on gross sales each week, then an array of valuable support services must be provided on an ongoing basis to meet the franchisee's changing needs.

3.1.3 Franchising Terminology

The potential value of any franchising arrangement is determined by the rights contained in the franchise contract. The extent and importance of these rights are quite varied. For example, a potential franchisee may desire the right to use a widely recognized product or name The term commonly used to describe this relationship between supplier and dealer is **product and trade name franchising**. Gasoline service and soft drink bottlers are typical examples. Alternatively, the potential franchisee may seek an entire marketing system and an ongoing process of assistance and guidance. This type of relationship is referred to as business format franchising. The volume of sales and number of franchise units owned through **business format franchising** have increased steadily since the early 1970s. Fast-food outlets and business services are examples of this type of franchising.

Piggyback franchising refers to the operation of a retail franchise within the physical facilities of a host store. Examples would be a Fix-It laundry is a franchise doing business inside Tops Supermarket. This form of franchising benefits both parties. The host store is able to add a new product line, and the franchisee obtains a location near the customers.

Another franchising strategy gaining widespread usage is **master franchising or subfranchising.** A master franchisor is an individual who has a continuing contractual relationship with a franchisor to sell its franchises. This independent businessperson is a type of sales agent. Master franchisors are responsible for finding new franchisees within a specified territory. Sometimes they will even provide support services such as training and warehousing traditionally provided by the franchisor. For example: C.P.Seven-Eleven is the master franchise of 7-Eleven in Thailand and Narai-Phan is his subfranchise who has the right to distribute 7-Eleven franchise system in northern part of Thailand.

Three types, or levels, of franchising systems offer opportunities for entrepreneurs. In system A, the producer/ creator (the franchisor) grants a franchise to a wholesaler (the franchisee). This system is often used in the soft-drink industry. Pepsi and Coca-Cola are examples of System A franchisors.

In the second level, designated as System B, the wholesaler is the franchisor. This system prevails among supermarkets and general merchandising stores. Tops super-market and Depot office center are examples of this system.

The third type, System C, is the most widely used. In this system the producer/ creator is franchisor and the retailer is the franchisee. Automobile dealerships and gasoline service stations are prototypes of this system. For example: Hung Pork noodle, Honda car.

To buy a franchise "Look before you leap" is an old adage that should be heeded by potential franchises. Entrepreneurial enthusiasm should not cloud your eyes to the realities, both good and bad, of franchising[1]. Therefore, we shall first look at the advantages of buying a franchise and then examine the limitations of franchising. The basic feature of the relationship between the franchisor and the franchisee are embodied in the franchise contract. The contract is typically a complex document, often running several pages. Because of its extreme importance in furnishing the legal basis for the franchised business, no franchise contract should ever be signed by the franchisee without legal counsel. As a matter of fact, many reputable franchisors insist that the franchisee have legal counsel before signing the agreement. An attorney would be useful in anticipating trouble and in noting objectionable features of the franchise contract. In addition to consulting and attorney, as a prospective franchisee you should use as many other sources of help as possible. In particular, you should discuss the franchise proposal with a banker, going over it in as much detail as possible. You should also obtain the service of a professional accounting firm in examining the franchisor's statements of projected sales, operating expenses,

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and net income. The accountant can give valuable help in evaluating the quality of these estimates and in discovering projections that may be unlikely to occur.

One of the most important features of the contract is the provision relating to termination and transfer of the franchise. Some franchisors have been accused of devising agreements that permit arbitrary cancellation. Of course, it is reasonable for the franchisor to have legal protection in the event that a franchisee fails to obtain a satisfactory level of operation or to maintain satisfactory quality standards. However, the prospective franchisee should avoid contract provisions that contain overly strict cancellation policies. Similarly, the rights of the franchisee to sell the business to a third party can assume ownership of the business at an unreasonable price. The right of the franchisee to renew the contract after the business has been built up to a successful operating level should also be clearly stated in the contract.

3.2 Current Trends in Consumer Behavior

The preceding historical perspective shows that successful companies adapt to changing consumer needs and environmental trends. The mid-1990s have seen equally important consumer behavior trends that will influence marketing strategies. Three in particular are a greater value orientation on the part of consumers, a desire for and access to more information and a desire for more customized products to fit consumer needs.

Steep recessions in the 1980s and 1990s have made consumers more price-sensitive. Today, with the realization that growth is not unbridled and that there are limits to future purchasing power, consumers are viewing price more in the context value, that is, getting your money's worth. The dichotomy makes sense in that consumers see value at both high price ends and low price ends in certain product categories. Greater sensitivity to value has led companies to keep prices down without sacrificing quality—one reason why companies are putting such great emphasis Total Quality Management (TQM).

Thais consumer is becoming a more aware and self-assured shopper. One reason is the greater accessibility of information and consuming options. The expansion of TV and media has make product information more available on the airwaves through home shopping channels, informecials (commercials that are almost program length), and an expanded advertising base. The greater incidences of home computers and advance in interactive technologies have expanded the availability of product information in cyberspace The strategic consequences of these changes on consumer behavior are yet to be felt. It is likely that marketers will expand the range of product options to consumers and insure that fuller product information is provided that is now typically the case. Marketers will also consider a broader range of media options in communicating to consumers in the future, and a broader range of delivery options as well (home shopping channels, telephone buying. electronic kiosks, buying on the Internet).

In Thailand. Pizza Hut recently introduce their new distribution channel that consumer can purchase their product via cybernetic or called as e-commerce, the millennium distribution channel of this decade.

A simple model of consumer behavior emphasizes the interaction between the marketer and the consumer. Consumer decision making –that is, the process of perceiving and evaluating brand information, considering how brand alternatives meet the consumer's needs, and deciding on a brand—is the central component of the model.

Two broad influences determine the consumer's choice. The first is the individual consumer whose needs, perceptions of brand characteristics, and attitudes toward alternative influence brand choice. In addition. the consumer's demographics, lifestyle, and personality characteristics influence brand choice. The second influence on consumer decision making is the environment. The consumer's purchasing environment is represented by culture (the norms and values of society), by subcultures (a part of society with distinct norms and values in certain respects), and by face-to-face groups (friends, family members, and reference groups). Marketing organizations are also part of the consumer's environment since these organizations provide the offerings that can satisfy consumer needs. During evaluation, the consumer will learn from the experiences and may change his or her pattern of acquiring information, evaluating brands, and selecting a brand. Consumption experience will directly influence whether the consumer will buy the same brand again.

A feedback loop also leads back to the environment. Consumers communicate their purchase and consumption experiences to friends and family. Marketers also seek information from consumers. They track consumer responses in the form of market share and sales data. However, such information neither tell the marketer why the consumer purchased nor provides information on the strengths and weakness of the marketer's brand relative to those of the competition. Therefore, marketing research is also requires at this step to determine consumer reactions to the brand and future purchase intent. This information permits management to reformulate marketing strategy to better meet consumer needs.

Brand attitudes are consumer's predisposition to evaluate a brand favorably or unfavorably. They are represented by three factors: beliefs about brands, evaluation of brands, and tendency to act. The assumption is that these components operate in sequence as follows:

1. Beliefs are formed about the brand that influence
2. attitudes toward the brand, which then influence
3. an intention to buy (or not to buy)

That is, if brand beliefs result in positive attitudes, there is a greater chance the consumer will buy the brand. For example, the belief that Pizza Hut is brand leader in Pizza market, dependable, and of high quality will result in a positive evaluation of their product. which in turn will increase likelihood that consumers will decide to buy it. An important link exists between benefits and attitudes. When beliefs about a brand conform to the benefits consumers' desire, consumers will evaluate the brand favorably. Favorable brand evaluation is more likely to lead to an intention to buy the brand.

Brand Loyalty represents a favorable attitude toward a brand resulting in consistent purchase of the brand over time. It is the result of consumers learning that one brand can satisfy their needs. Several researchers have attempted to define the characteristics of a brand-loyal consumer, that is, a consumer who tends to be loyal regardless of product category. Brand loyalty is product-specific. Consumers will be loyal to brand in one category and will have little loyalty to brands in other categories.

Despite the product-specific nature of brand loyalty, some generalizations can be made about those who tend to be brand loyal:

1. The brand-loyal consumer tends to be more self-confident in his or her choice. Both day and Carman found this relationship to be true in separate studies of consumer packaged goods.
2. Brand-loyalty consumers are more likely to perceive a higher level of risk in the purchase and use repeat purchasing of a single brand as a means of reducing risk.

3. The brand-loyalty consumer is more likely to be store-loyal. Carman states that the consumer who restricts the number of stores visited thereby restricts the opportunity to be disloyal to the brands the store sells. Therefore "store loyalty is a regulator of brand loyalty".
4. Minority-group consumers tend to be more brands loyal. Some studies have found that African-American and Hispanic American consumers tend to be more brands loyal. Loyalty may be the result of greater financial risk in purchases and a desire to "play if safe".

The cognitive definition of brand loyalty means that loyalty represents commitment and therefore, involvement with the purchase. A study by J.Walter Thompson, a large advertising agency, found that loyalty is highest when consumers are personally involved with the brand and find the purchase risky.

The important component in the communications model is message transmission. Marshall McLuhan's statement, "The medium is the message," implies that the media communicates an image independent of any single message that is being transmitted. The media environment influences consumers' reaction to a communication in two ways. First, particular types of media such as magazines may influence message evaluation. Magazines such as the New Yorker, Reader's Digest, and Playboy have different images based on different editorial content, reputation, and subscribers. Second different types of media (magazines versus television, for example) influence consumers' reaction message.

3.3 Advantage and Disadvantage of Franchising from Franchisee Point of View

The choice of franchising over alternative methods of starting your own business ultimately is based on adding up the pluses and minuses of franchising after considering the entrepreneur's personal goals and aspirations (Table4.1). Franchising obviously will not be the choice for all prospective entrepreneurs, because each consideration will carry different weight for different individuals. However, in their particular circumstances, many people find the franchise form of business to be the best choice.

Table 3.1: Major Plus and Minus in the Franchising Calculation

+ PLUSES	- MINUSES
Formalized Training	Franchise Fees
Financial Assistance	Royalties
Proven Marketing Methods	Restrictions on Growth
Managerial Assistance	Less Independence in Operations
Quicker Startup Time	Franchisors May Be sole Supplier of some supplies
Overall Lower Failure Rates	
Termination/ Renewal Clauses	

A franchise is attractive for many reasons. Three advantages in particular warrant further analysis. A franchise can offer the entrepreneur (1) formal training, (2) financial assistance, and (3) marketing and management benefits. Naturally, all franchises may not be equally strong on all those points. But it is these advantages which motivate many persons to consider the franchise arrangement.

1. **Formal Training**: The importance of formal training received from the franchisor is underlined by the managerial weakness of many small entrepreneurs. To the extent that this weakness can be overcome, therefore, the training program offered by the franchisor constitutes a major benefit.

   - Initial Training
   - Continuing Guidance

The value and the effectiveness of training are evident from the records of business failures, a large majority of which are caused by deficiencies in management. For example. franchisors such as MK Suki and restaurant, McDonald's and Kentucky Fried Chicken have well training to their employee. Some franchisors admit to purchasing a weak operating franchisee to keep it from going under, thereby maintaining their image. However, there appears to be little question that the failure rate for independent small business in general is much higher than for franchised businesses in particular.

Operate as a franchisee, however, in now way guarantees success. A particular franchisor may offer unsatisfactory training. The franchisee may not apply the training correctly or may fail for some other reason.

1.1 Initial Training: Training by the franchisor often begins with an initial period of a few days or a few weeks at a central training school or at another established location. For example MK Suki and Restaurant operate the training center of their own. The program cover not only the operating procedures to be used by the business, but also broader topics such as record keeping, inventory control, insurance, and human relations.

The Mister Donut franchise requires an initial training course of four weeks, including such topics as donut making, accounting and controls, advertising and merchandising, scheduling of labor and production, purchasing, and so on. Naturally, the nature of the product and type of business affect the amount and type of training required in the franchised business. In most and permits individuals who have had little training and education to start and succeed in business of their own.

1.2 Continuing Guidance: Initial training is ordinarily supplemented with subsequent training and guidance. This may involve refresher courses and/or training by a traveling representative who visits the franchisee's business from time to time. The franchisee may also receive manuals and other printed materials that provide guidance for the business. However, guidance shades into control, so that in particular it may be difficult to distinguish the two. The franchisor normally places a considerable emphasis upon observing strict controls. Still, much of the continued training goes far beyond the application of controls. While some franchising systems have developed excellent training programs, this is by no means universal. Some unscrupulous promotes falsely promise satisfactory training.

2. **Financial Assistance**: The costs of starting an independent business are often high and the prospective entrepreneur's sources of capital quite limited. The entrepreneur's standing as a prospective borrower is weakest at this point. By teaming up with a franchising organization, the aspiring franchisee may enhance the likelihood of obtaining financial assistance.

If the franchising organization considers the applicant to be a suitable prospect with a high probability of success, it frequently extends a helping hand financially. For example, the franchisee seldom is required to pay the complete cost of establishing the business. In addition, the beginning franchisee is normally given a payment schedule that can be met through successful operation. Also, the franchisor may permit delay in payments for products or supplies obtained from the parent organization, thus increasing the franchisee's working capital.

3. **Marketing and Management Benefits**: Most franchised products and services are widely known and accepted. For example, customers will readily buy McDonald's hamburgers Baskin-Robbins ice cream or MK Suki because they know the reputation of these products Travelers may recognize a restaurant or a hotel because of its name, or some other feature The travelers may turn into a Starbucks coffee or a Holiday Inn because of their previous experience and the knowledge that they can depend upon the food and service that these outlets provide. Thus, franchising offers both a proven successful lines of business and product or service identification.

The entrepreneur who enters a franchising agreement acquires the right to use the franchisor's nationally advertised trademark or brand name. This serves to identify the local enterprise with the widely recognized product or service. Of course, the value of product identification differs with the type of product or service and the extent to which it has received widespread promotion. In any case, the franchisor maintains the value of its name by continued advertising and promotion.

In addition to offering a proven successful line of business and readily identifiable products or services, franchisors have developed and tested their methods of marketing and management. The standard operating manuals and procedures they supply have permitted other entrepreneurs to operate successfully. This is one reason why franchisors insist upon the observance of standardized methods of operation and performance. If some franchises were allowed to operate at substandard levels, they could easily destroy the customer's confidence in the entire system.

The existence of proven products and methods, however, does not guarantee that a franchised business will succeed. For example, what the franchisor's marketing research techniques showed to be a satisfactory location may turn out to be inferior. Or the franchisee may lack ambition or perseverance. Yet the fact that a franchisor can show a record of successful operation proves that the system can work and has worked elsewhere.

In particular, three shortcomings permeate the franchise form of business. These are (1) the cost of franchise, (2) restrictions on growth that can accompany a franchise contract, and (3) the loss of absolute independence on the part of the franchisee.

1. **Cost of a Franchise**: the total franchise cost consists of several components. Only after all of these cost components have been examined can a realistic picture be drawn. The additional cost of a franchise, which differs from other independent store, begins with the franchise fee. Generally speaking, higher fee will be required by the well-know franchisors.

2. **Restrictions on Growth**: A basic way to achieve business growth is to expand the existing sales territory. However, many franchise contracts restricts the franchisee to a defined sales territory, thereby eliminating this form of growth. The potential franchisee, therefore, should weight territorial limitation against the advantage cited earlier.

3. **Loss of Absolute Independence:** Frequently, individuals leave salaried employment for entrepreneur because they dislike working under the direct supervision and control of others. By entering into a franchise relationship, such individuals may simply find that a different pattern of close control over personal endeavors has taken over. The franchisee does surrender a considerable amount of independence upon signing a franchise agreement. Even though the franchisor's control of business operations may be helpful in assuring success, regulation may be unpleasant to an entrepreneur who cherishes independence. In addition, some franchise contracts go to extremes by covering unimportant details or specifying practices that are more helpful to others in the chain than to the local operation. Thus, as an operator of a franchised business, the entrepreneur occupies the position of a semi-independent businessperson.

In making a decision whether or not to embark upon a franchised business, an assessment has to be made of the advantages and disadvantages of franchising from the franchisee's point of view compared with a non-franchised business. The advantage of franchising for a franchisee are summarized commonly underneath:

Advantages to the Franchisee:

1. The franchisee's lack of basic or specialized knowledge and experience is over come by the training program of the franchisor.

2. The franchisee has the incentive of becoming the owner of a business supported by the assistance from the franchisor. Franchisee is called as an independent business who run the business within the framework of the franchise agreement and able to effort maximize value of the investment by himself.

3. The franchisee's business opens with the benefit of a name and reputation (a brand image) and goodwill, which is already well established in the consumer perception. This may reduce the lead-time to creating market recognition and business successful. The franchisee has the benefit of the use of the franchisor's patents, trademarks, trade name, trade secret and business format.

4. The franchisee should receive assistance in:

   (a) Location selection

   (b) Operate plan

   (c) Financial assistance for the acquisition of the franchised business

   (d) Formal training

   (e) Purchasing equipment and merchandise inventory

Note: More information about franchisor support explains in Chapter3

5. The franchisee receives the benefit on a national scale (if appropriate) of the franchisor's advertising and promotional activities.

6. The franchisee receives the benefit of the bulk purchasing and negotiating capacity of the franchisor on benefits to the size of operation.

7. The risks of business failure are substantially reduced. However, no franchisee should consider that under the umbrella of the franchisor there is no risk at all. All business undertaking involves risk, and a franchised business is no exception. To be successful, the franchisees have to work hard and concentrate to their business. The franchisor will never guarantee great rewards for little effort.

8. The franchisee has the right to obtain services of troubleshooters or field operational staff provided by the franchisor in the time of operation problem.

9. The franchisee gain benefit of the franchisor's continuous research and development programs to improve the business and keep it up to date.

Disadvantages to the Franchisee:

1. Inevitably the relationship between the franchisor and franchisee will involve the imposition of controls. These controls will regulate the quality of the products and services, which distributed by franchisee. The franchisee have to get along the franchisor regulation because it is not lead to his success only but also indirect to their brand name.
2. The franchisee will have to pay the franchisor for the services provided and for the use of the blueprint i.e. franchise fee, royalty fee.
3. The difficulty of assessing the quality of the franchisor.
4. The franchise contract will contain some restrictions against the sale or transfer of the franchised business. Further the franchisor may require a substantial payment for the business transferred.
5. The franchisees may find they becoming too dependent upon the franchisor. This reason can motivate franchisee to create their business to obtain higher profit.
6. The mistaken or insolvency cf the franchisor will directly affect the franchisee's operation.

3.4 Advantage and Disadvantage of Franchising from Franchisor Point of View

Franchising contains opportunities on both sides of the fence. We have already presented the franchising story from the viewpoint of the potential franchisees. Now we shall briefly look through the eyes of the potential franchisor.

Advantages to Franchisor:

Why would a businessperson wish to become a franchisor? At least three general benefits can be identified.

1. Reduced capital requirement: Franchising allows us to expand without diluting our capital. The firm involved in franchising, in effect, through fee and royalty arrangements, borrows capital from the franchisee for channel development and thus has lower capital requirements than does the wholly owned chain.

2. Increased management motivation: Franchisees, as independent businesspeople, are probably more highly motivated than salaries employees because of profit incentive and their vested interest in the business. Since franchising is decentralized, the franchisor is less susceptible to labor-organizing efforts than are centralized organization.

3. Speed of expansion: Franchising lets a business enter many more markets much more quickly than it could using only its own resources.

Disadvantage to Franchisor:

There are also distinct drawbacks associated with franchising from the franchisor's perspective. At least three of these can be isolated:

1. Reduction in control: A franchisor's right of control is greatly reduced in the franchising form of business. This is a major concern for most franchisors.
2. Sharing of profits: Only part of the profit from the franchise operation belongs to the franchisor.
3. Increasing operating support: There is generally more expense associated with nurturing the ongoing franchise relationships-providing accounting and legal services-than there is with centralized organization.

Franchising has undoubtedly enabled many individuals to enter business who otherwise would never have escaped the necessity of salaried employment. Thus, franchising has contributed to the development of many successful small businesses.

3.5 The Key of Success and Failure in Franchise

Since the booming of franchise in Thailand many new franchises brand names are launched into the market especially the new comer SME. Some still exist in the market some disappeared. This topic will analyze the key of success and failure in franchise business.

The business format franchise involves the exploitation not merely of goods identified by a brand name or an invention, but the preparation of the "blueprint" or "system" or "package" of a successful way of carrying on a business in all its aspects. The system must have been so carefully prepared as to minimize the risks inherent in opening any new business. The franchisor will have prepared and smoothed the way for a person. who has probably never owned or operated a business before, to open up a business of his own not only with a predetermined and established format but within the backing of and organization which would not otherwise be available to him.

Each franchised business, which is successful, has its own innovation concept, which sets it apart from other businesses of the same type. It is also important that the trade secret is carefully designed and the franchisor should devise the efficient strategies to protect it.

The empirical evidence that support the importance of the franchise system is given below.

The Pizza Public Company Chairman William E.Heinecke gave some comments of Pizza Hut's success as follows:

"One of the reason why Pizza Hut is a success for us is their system. In franchising it's not so much the name-you need the product and the system to make it work. Pizza Hut has the system and the training program which help to make it work."[1]

There are several elements involved in franchise system. This study will focus to those, which are in accordance with the franchise contract.

When the franchisor decides to expand and existing business by means of the franchise system, he has to keep the business simple. The more complex it is the more difficult it will be to recruit train and sustain franchisees. In the case of food operation, there is also the paramount need to keep the menu simple. This reduce the requirements of the skilled cook and make its possible to keep preparation of the food simple, quick and efficient. In the case of Pizza Hut (Thailand), the central kitchen was established to prepare the ingredient of their product to all outlets in order to control the product's quality.

The obstacle to grant a franchise of restaurant franchise is the nature of the food and the strategy to protect the trade secret. Because of the variety of the menu and no automatic equipment to produce food to the same standard, the franchisor felt that the appropriate way to control the standard of food was to send staffs who were trained by the franchisor to the franchised outlet.

Moreover, it the franchisee and his staff could operate the cooking by themselves, he may feel that he needs not to depend on the franchisor and would be reluctant to pay the royalties every month. He then may not renew the contract and open a competing business after the contract termination. Many franchisors control the standard of food and the sales volume by sending staff to the franchised outlet, this conduct is not appropriate to the franchise concept.

The franchisee should have the full authority to manage his store under the same standardization without the franchisor's staff to control him all the time. The franchisor should provide an appropriate number of products' item because the product's variation increase the complexity and difficulties for cooking and/or operating, and demanding for the cook's skill. They should also invent efficient strategies to protect the trade secret. Foreign fast food franchises protect their trade secret by supplying the mixed ingredient such as the mixed flour to make pizza or donut.

One indicator of the system's preparation is the operational manual. The operational manuals are the essential part of the process whereby the franchisor transfers to the franchisee his know-how relating to the running of the franchised system. The empirical evidence discovered that the foreign franchisors given paramount importance to the operational manuals while the local franchisors did not. For example, KFC has the following manuals: KFC Menu Board System, KFC Corporate Identity Standards, AID's Marketing Manual, Quick Service Restaurant Study (Management Summary). McDonald's provides the business manuals containing detailed information relating to operation including:

(1) Food formulas and specifications for designated food and beverage products
(2) Methods of inventory control
(3) Bookkeeping and accounting procedures
(4) Business practices and policies
(5) Other management, advertising, and personal policies.

Many local franchisors do not provide operational manuals. Some local franchisors admitted that their operational manuals were not complete enough and they want to improve them to meet international standards.

The franchisors should prepare the staff to support the franchisees whenever they face difficulties in doing business. The franchisor's troubleshooter should also be available at all times to the franchisee when required. The surveyed evidence found that many franchisees of foreign franchise appreciated the assistance of franchisors' troubleshooters.

They can phone to the troubleshooter at all time if they have problems. When the problem is serious, the troubleshooter will come to Thailand to help them. Some of local franchisors accepted that one major cause of their failure in granting a franchise is the lack of potential staff to support their franchisees. Some franchisees of a local laundry business comment that their franchisor never support their business for example when the washing machine was out of order, the franchisor did not send any technicians to fix it.

One of the important aids is sending franchisor's opening teams to help the franchisee during the initial time to make sure that the franchise package is implemented successfully. For example, empirical evidence found that Dunkin Donut sent the opening team to stay with the franchisee for three months, Burger King: one-two months, 7-Eleven: one month (six staff)

It is essential to have a proven, identified success before commencing franchising. At least one pilots operation, and probably in many cases a number of pilot operations, should be established. 7-Eleven is a good example in the case. Due to the abundant capital of the CP Group, it is able to invest a large number of company-owned outlets to establish a firm base and create the brand image and goodwill to the public before granting a franchise.

The training is the process that a franchisor transfers his know-how and success to the franchisee. The training to be provided by the franchisor is perhaps from the franchisee's point of view the most important part of the franchise agreement. The type of training to be provided will obviously vary greatly with different types of franchise. In short, the franchisee expects to have imparted to him all the skills necessary to operate his business satisfactory from the outset.

The most difficult task of franchise scheme is maintaining the interdependent relationship through the contract's term. The franchisor's main task is maintaining the brand image and goodwill by various methods. First, there must be control of all outlets to be of the same standardization, a crucial characteristic of the franchise system. One outlet that provides a lower standard of product and/or services to the customers can save costs. But eventually the cost is borne by all other units, which lose the customer's patronage.

The franchisors control the externalities and free-rider behavior of the franchisees by inspecting the outlets both advanced informing or non-informing. Some franchisors employ the method of the mysterious shopper who pretends to be and ordinary customer to see whether or not the standard of products and services is maintained.

The franchise fee is also a major factor to consider for a potential franchisee. If the franchise fee is too high compared with the benefit he will get, or he may not take a franchise. Consequently, a franchisor cannot expand franchising up to the setting target.

The franchisee obtains many benefits from franchising such as the benefit of a brand image and goodwill, know-how, continuous services, national scale of advertising and promotion activities, bulk purchasing and negotiating capacity of the franchisor on behalf of all franchisees, and so on. Although the franchisor gets the benefit from the franchisee's local knowledge, he has costs to support and control all franchisees and to maintain the brand image through nationwide promotion and advertising. No franchisor is going to give anything away for nothing. Payment is made to the franchisor in any number of ways. There are a number of different ways in which a franchise fee may be charged, and its is possible that franchise fee will be payable in more than one of the ways described. The example of various methods by which a franchise fee is taken is an initial franchise fee, sale of products. Whichever way the fees are to be taken by the franchisor, he will be paid both for his initial services and for the continuing services that he provides. The franchise fee should also be designed to motivate the franchisor and the franchisee to be efficient. The survey evidence suggests that the appropriate franchise fees should consist of an initial lump sum fee and continuing fees (royalties or sales of products). The initial franchise fee should not be unrealistically high. It should be a fairly modest sum of money and represent the expenses the franchisor incurs to help the franchise start the business. The continuing fee is essential since it gives the franchisor incentive to be efficient in ongoing services.

Advertising is another device to maintain the reputation of brand name and customer's awareness. The franchisor invariably will run international and local advertising schemes and also ensures that the important field of public relations is looked after. In the case of the foreign franchise, advertising and promotion in Thailand will be the franchisee's responsibility. The franchisee shall use advertising and promotional materials and programs provided by the franchisor or approved in advance by the franchisor. Some franchisors will force the franchisee (through the franchise agreement) to expend a certain sum during each calendar year for advertising and promotion. It is usually and amounts not less than a particular percentage of the gross sales, for example 4% of gross sales per annum.

The franchisee's behavior is the chief factor in achieving success. He has to operate under the same standardization of the franchise system. The externalities and free-rider behavior not only harms him in the long run but also all outlets of the franchise chain. This behavior is an obstacle for franchising. Some master franchisees considered that it might be too early for Thai small businessman to realize the importance of goodwill and reputation of brand name in the long run more than profit making over a short period. Consequently, McDonald's and Minor Holding Group have no policy to grant sub-franchises.

After being trained and helped to set up and run the business successfully, the franchisees tend to develop a feeling of independence. He wonders why he needs the franchisor at all. He becomes convinced that the reason for his success is that he is running his business well on his own initiative. He is reluctant tc pay royalties to the franchisor. He will not operate the business under the same standardization of the franchise system.

This situation happened to Central minimart and many franchisors in Thailand. In 1991, two franchisees did not follow Central's standard such as shelf display and personnel management, affecting the brand images and staffs incentive to work efficiently. Moreover, they delayed the payment of goods that they ordered from suppliers in the name of Central. Central withdrew the franchise agreement and halted granting franchise rights until the contract, the system and the perscnnel were improved. In addition, future franchisees will have no right to manage the outlets; the management will be under Central staff. If the franchisee wants to have a part in management. he or his representative has to be an employee of Central. If he cannot operate the business successfully, he will be transferred or receive some form of punishment like ordinary staff.

In the author's opinion, Central's strategy to prevent the problem of externalities is not in accordance with the franchise concept. The franchisee should have the right o operate his outlets. Central should prepare an efficient strategy and staff to control the franchisee and invent the benefit from franchising to induce the franchisee.

The franchisee should adapt local knowledge to operate the business in order to serve Thais consumer. It is unlikely that an effective strategy, which operates well in one country, will work in another. Markets and environments are different. The franchisee should take these differences into account and tune them to match the Thais. For example, Pizza Hut presented

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20) Unreasonable pressure to sell franchises

21) Unworkable economic relationship with franchisees

22) Lack of effective compliance systems

23) Royalty underpayment/ nonpayment by franchisees

24) Operational systems that can be easily duplicated

25) Lack of effective financial controls

26) Lack of experienced management

27) Unprotected trademarks

28) Excessive litigation with franchisees

29) Inadequate training program

30) Decentralized advertising

31) Lack of ongoing research and development

32) Unbridled geographic expansion

33) Choice the wrong subfranchisors

34) Unprofitable and unhappy franchisees

35) Lack of public relations

36) Unwillingness to enforce franchise agreement

37) Inadequate relationship with key vendors

38) Improper earnings claims

39) Premature terminate of franchisee

40) Lack of market research