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1. Agency Costs, Search Costs, Transactions Costs, Managerial Limits to Firm Growth and New Franchisor Survival 1984-1994

Scott Shane, Massachusetts Institute of Technology

Chester Spell, Georgia Institute of Technology

This study explores the survival of new franchise systems created in the United States between 1981 and 1983 over the period 1984-1994. Using longitudinal data, the paper links together disparate theories of franchising to argue that new franchisors which minimize agency, transaction and search costs, and which quickly build their brand names and overcome managerial limits to growth are more likely to survive. In specific, the paper shows that new franchisor survival depends on rapid growth of outlets to lower the cost of promoting a new system's brand name. By allocating local market activity to franchisees, new franchisors can overcome managerial limits to firm growth and establish outlets fast enough to reach minimum efficient scale to promote their brand names competitively with established firms. By signaling non-opportunistic tendencies and high quality of intangible assets, the new franchisor can attract franchisees quickly enough to avoid master franchising, which undermines the high powered incentives of franchising.

2. Franchising Growth in the U.S. Market: Myth and Reality

Francine Lafontaine, University of Michigan

Kathryn L. Shaw, Carnegie Mellon University

This paper discusses franchising growth, and how it is captured by franchisor entry and exit. It shows that business-format franchising in the U.S. has not been growing at the kind of formidable rate that the press often suggests. Rather, while many new firms enter into franchising each year, giving this impression of tremendous growth, many are also exiting, leading to an overall growth at best commensurate with that of the economy. Also, consistent with existing literature, we show that franchisor exits are unrelated to most initial characteristics of the chain as described in major franchisor directories. Given the impact franchisor exit must have on franchisee success, it is disconcerting to find so much of it, and have so little capacity to predict it. We suggest that future work on franchisor exit should focus on less easily available data on such things as product offerings, franchisor support capabilities and its principals' human and financial resources to shed more light on factors affecting the success and failure of franchisors.

3. Franchising as a Growth Strategy in the U.S. Restaurant Industry

Kabir C. Sen, Lamar University

Although franchising has been postulated to be a solution to resource constraints, there has been little past research on the linkage between franchising and firm growth. The paper therefore develops predictions about the use of franchising as an expansion strategy and examines them through an empirical investigation of a sample of restaurant franchisors. The restaurant industry is an appropriate field for such an investigation as franchising is extensively used in this sector. The results suggest that franchising is an effective strategy for store expansion. There is also support for a life cycle pattern in the use of franchising with larger chains showing a lower need for franchising as a growth strategy.

4. Franchise Growth and Failure in the U.S. and the U.K., A Troubled Dreamworld Revisited

John Stanworth, University of Westminster, London, England

David Purdy, University of Westminster, London, England

Stuart Price, KPMG, London, England

The literature on franchising has often separated out into two camps. Franchisors and their trade organizations have typically been very buoyant concerning the activities and prospects of franchising. Academics, for their part, have usually shied away from the more contentious debates and, instead, focused their attentions on either pragmatic operational issues or, alternatively, conceptual theoretical discourse. This current paper discusses two contentious issues, largely overlooked by academics until relatively recently but currently moving centre-stage. We refer here to the issues of franchise growth and survival rates. The paper examines recent research on these issues from both the U.S.A. and the U.K. and concludes that a growing body of evidence suggests the need for a radical re-appraisal of the risks and challenges associated with franchise system development.

5. Franchising as a Tool for SME Development in Transitional Economies: The Case of Central European Countries

Nitin Sanghavi, The University of Manchester, London

It is generally acknowledged that franchising plays an important role in furthering the development of the Small Medium Sized Enterprises (SME) sector. In several Central European countries, franchising is already well known and has an increasing role in national economies. In some developing countries, franchising has been adopted by national governments as one of the strategies for faster economic development and is considered a major tool for developing consumer markets as well as supply chain and provides faster job creation and new incomes in the SME sector on a sustainable basis where micro enterprises are the prevailing entities.

However, it should be pointed out that the successful development of franchising depends on the overall economic development process and cycle of the transitional economies.

This paper explores these issues by discussing benefits as well as limitations in using franchising as a tool for SME development in transitional economies in general and the case of Central European countries in particular. It highlights key issues and challenges and identifies areas for further research.

6. Panel Discussion. Franchise Education Programs and Other Initiatives Premier FastTrac®; National Franchising Initiative of the Association of Small Business Development Centers; Fair Franchising Standards of the American Association of Franchisees...

Moderator: Cheryl R. Babcock, CFE, University of St. Thomas Panelists: Ann Dugan, University of Pittsburgh Stuart Monroe, Entrepreneurial Education Foundation Peter Stern,

NatWest Bank, London

7. Fast-Food Franchises and Supercenters: A Tale of Two Alliances and Beyond

Joyce Young, Indiana State University

Audhesh K. Paswan, University of South Dakota

John M. Buch, Indiana State University

Lori Ashby, Indiana State University

Co-marketing and co-branding agreements are international growing trend in the franchising industry. To date, the relational properties these relationships are not well documented in the franchising literature. This paper attempts to begin fill this void by the examination of the most visible co-marketing alliances: 1) McDonald's/Wal-Mart, and 2) Little Caesars/Kmart.

8. Franchisees Roaming Across the Field of Paradoxes

Matti Koiranen, University of Jyväskylä, Finland

Kimmo Hyrsky, University of Jyväskylä, Finland

Mika Tuunanen, University of Jyväskylä, Finland

The present paper shows that the world of franchisees comprises paradoxical features. Paradoxes are tenets or propositions that are contrary to received opinion. Often they are also statements or sentiments that are seemingly contradictory, self-contradictory or opposed to common sense. We set out to analyse some perceived advantages, disadvantages and entrepreneurial characteristics of Finnish franchisees. In our quantitative study of 686 respondents, the advantages that franchisees regarded as the most relevant were: `Known Company Name or Trade Mark´, `Proven Business Concept´, `Economics of Scale´, `Franchisor Support´, `Greater Job Satisfaction´ and `Opportunity for Family Business´. The perceived disadvantages included: `Fees´, `Excessive Working Hours´, and `Contractual Issues´. Furthermore, it appeared that franchisees regarded themselves as customer-oriented people who shoulder responsibility for their own actions and badly want success in their current businesses.

The results displayed the highly dynamic nature of a satisfactory franchisor-franchisee relationship. It was found that support given by the franchisor may gradually lose its value if it is not consistently updated and renewed. Thus, for instance, franchise fees often started to become, first a source of dissatisfaction, and later even a potential source of conflict. Finally, paradoxicalness was discovered in the empirical analysis of the advantages, disadvantages, and entrepreneurial characteristics. The contradicting results implied, for instance, that an original advantage is gradually turning into a disadvantage.

9. Franchising in the West Meets the East: A Discriminant Approach...

Skip Swerdlow, University of Nevada-Las Vegas W. Thedore Cummings, University of Nevada-Las Vegas

Dianne H.B. Welsh, Eastern Washington University

Nicholai Bushmarin, Tver State University, Russia

The continuing expansion of the hospitality industry into international markets, especially the Russian Federation, has been challenged by their unstable and often criticized transition to a regulated market economy. Yet among the many industries that have penetrated this market, lodging has appeared to garner the greatest success. In spite of these successes, hospitality franchises have continued to face human resource challenges. The challenges arise out of the differences between Eastern and Western culture, expectations, and economic and political history. While franchise organizations may get their operational and physical structure in place, one of the areas over which they have limited control is employee attitudes. The question then is, how Russian managers and employees differ in their attitudes about the work environment. The purpose of this research, therefore, is to compare Russian and American hotel managers and employees on selected organizational behavior variables, specifically job satisfaction and organizational commitment, and to assess the impact of these differences on lodging franchise organizations that are considering entering the Russian hospitality market. There are several conclusions that can be drawn from this research. The first is that descriptive analysis demonstrates that Russian hotel employees are different from their American counterparts. The issue of job satisfaction further confirms this conclusion; it is that job satisfaction is different between hotel workers in both the U.S. and Russia. Franchisors may not make the assumption that successful formats for operational quality, training, team building, and other human resources issues will easily fit the Russian employee. These findings imply that what has evolved and works in the U.S. franchise organizations may not be directly transferable into the Russian lodging industry without modification.

10. Having Your Cake and Eating it Too!

Wilke English, The University of Mary Hardin-Baylor

Robert Justis, Louisiana State University

From a simple handshake and a "let's clone this business" attitude, the phenomena of franchising has grown ever more complex. In fact, it has grown so complex, and so expensive, that many entrepreneurs avoid the franchising route entirely.

This exploratory paper explores the complex legalities of franchising in several areas:

1. Why is it better (for the franchisor) to have franchisees than distributors?
2. What makes a business opportunity (legally) a franchise?

   and most importantly:

3. Can you have your cake and eat it too?
   Can you set up a business opportunity so that it retains the advantages of franchising (control and franchisee investment) while avoiding the official definition of a franchise, and hence the expense of registering as a franchise?

   This paper created eight scenariors 'scenarios' in which an erstwhile entrepreneur has tried to create a business opportunity which will avoid the official definition of a franchise. The paper then presented an assessment of how each might be viewed by the regulators.

11. To Own … Or … Not to Own?

Audhesh K. Paswan, University of South Dakota

As a franchise system moves further into its life-cycle, the franchisor would have more funds and manpower talent available, and at this stage, there will be a tendency to shift towards corporate ownership (Oxenfeldt and Kelly's 1968-69). However, the empirical evidence at best provides a mixed support for this notion. It seems to point towards a more pluralistic perspective, i.e., different levels of company and franchisee owned units may coexist in different franchise systems. This study suggests a continuum of ownership mix where franchisor dominant systems fall in at one end and the franchisee dominant systems at the other. Included among this continuum are several somewhat distinct points, of which ownership redirection in favor of franchisor is but one option. The underlying basis is that if the primary goal of franchisor is to grow in size and become flush with funds, then these objective can be accomplished through any one of the several ownership mix options.

12. The Characteristics of Multi-Unit Ownership in Franchising: Evidence from Fast- Food Restaurants in Texas

Artus Kalnins, University of Michigan

Francine Lafontaine, University of Michigan

One empirical phenomenon that has received little attention in the franchising literature is the tendency for individual franchisees to own not just one but several units of a given franchised chain. Most current theories of franchising, based on incentives, information asymmetries, and strategic arguments, have little capacity to explain this phenomenon. In fact, several of them imply that all units should be independently owned and operated. However, given the existence of multi-unit owners, most of the theories have implications for the extent to which units owned by a single owner should be 1) geographically near each other, 2) located in areas where populations display similar demographic characteristics, and 3) contiguous to each other, or share a market boundary.

This paper provides empirical evidence that restaurants of individual owners in the six largest fast-food chains in Texas are geographically close to each other, that they are located in areas with similar demographic characteristics, and that they are contiguous. This evidence suggests among other things that franchising is not a strategic delegation device, and that the location of units is not determined by the franchisee's desire to diversify away risk. Instead, the minimization of monitoring or free-riding costs, and the franchisor's reliance on the franchisee's local market expertise, appear to be central concerns in the allocation of units across franchisees.

13. The International Distribution of Franchises by U.S. Franchisors

Dixie S. Zietlow, University of Michigan

Jean-Francois Hennart, University of Illinois- Chicago

The objective of this study is to analyze how US franchisors develop their franchise distribution systems in foreign countries. There are six main methods used by franchisors to distribute their franchises overseas. They may own a wholesale distributor by making an investment in a wholly-owned subsidiary or a joint venture. Alternatively, US franchisors can sign a contract with an independent wholesale distributor called a sub-franchisor or area developer. Or they can bypass the wholesale stage altogether and go directly to the retail stage making an investment in a company-owned unit or signing a contract with a franchisee.

Internationalization, marketing, transaction cost, and capitalization theories suggest how cultural and physical distance, international experience, cost of capital and market size should affect the type of foreign distributor chosen by the US franchisor. The hypotheses were tested on a sample of 455 wholesale and retail distribution agreements made in over 85 countries by 46 US franchisors in the food service, hotel/motel, and business service industries.

14. Accounting Profit or Economic Profit: The Impact of Alternative Objectives on the Decision to Franchise

Patrick J. Kaufmann, Georgia State University

Richard M. Gordon, University of Florida

James Owers, Georgia State University

Analysis of the decision to franchise has assumed that the franchisor is seeking to maximize the long term economic value of the firm. In this paper, an alternative objective function is proposed, one that seeks to maximize those performance measures arguably favored by the financial markets, i.e., accounting value measures. A simple model of franchisor performance is developed and several scenarios of franchise system expansion examined. Decisions to open franchised or company owned outlets are compared using the competing objective functions.

15. Encroachment: An Analysis of the Situation-Past, Present and Future

William Slater Vincent, Kennesaw State College

One of the hottest issues today in franchising is that of encroachment. On the one hand the franchisor must continually expand its system in order to increase its market share and maintain its competitiveness. On the other hand a franchisee who has a large sunk investment in its franchise wants to enhance its financial stability and minimize negative impacts. A franchisee, as a business owner, recognizes that it will face negative impacts in the form of competition from other systems. However, what has a franchisee up in arms is when its business, is negatively impacted through the expansion of its own franchisor at its expense. A franchisee feels that it shouldn't have to compete with itself. This paper explores the issue of encroachment covering what has occurred in the courts and on the legislative and regulatory fronts with how franchisors are addressing the issue.

16. Influence of Franchisee Selection Criteria on Franchisee Performance

Thani Jambulingham, University of Wisconsin

John Nevin, University of Wisconsin

Agency theory suggests that an efficient contract between a franchisor (principal) and a franchisee (agent) could be established by the use of selection criteria that would screen prospective franchisees based on their likely future performance, thus minimizing the precontractual problems. Franchisee selection criteria can serve as a key input control mechanism by franchisors desiring to enhance the performance of their future franchisees and reduce long-term monitoring costs. This article examines the relationship between key franchisee selection criteria such as franchisee attitudes towards business, financial capability, experience and management skills, demographic characteristics, and key measures of franchisee performance. The findings show that franchisee attitudes toward business can be used as an effective input control strategy by franchisors because they explain a substantial portion of the variance in franchisee performance.

17. Panel Discussion. The Effects of Changes in the Global, Social, Political and Legal Environment on Franchise Performance: A European and North American Comparison

Co-moderators: Dianne H.B. Welsh, Eastern Washington University Cecilia M. Falbe,

University at Albany-SUNY Panelists: Philip Mark Abell, Field Fisher Waterhouse, London Colin Foley, Gilchrist and Company, Glasgow Alex Konigsberg, Goodman Lapointe Ferguson, Montreal

18. A Longitudinal Analysis of Transaction Costs in Franchised Distribution Channels

Robert Dahlstrom, University of Kentucky

Arne Nygaard, Norwegian School of Management

This study examines the dynamic influence of organizational control mechanisms on transaction costs. The authors present a model which suggests that interorganizational interaction, formalized procedures, and opportunism influence bargaining, control, and maladaption costs. A test of the model using time series data from the Norwegian oil industry indicates that interaction curbs bargaining costs and formalization reduces control and maladaption costs. By contrast, opportunistic behavior increases bargaining, control, and maladaption costs. Implications for franchising management and theory are discussed.

19. Franchise Systems in Distant Markets: Control Techniques and Upward Flow of Information

Rajiv Dant, Boston University

Nada Nasr, Boston University

Information exchange between franchisees and franchisors is viewed as instrumental for the attainment of both firm-specific and systemic goals within franchise systems. Our study investigates the issue of *control* and control techniques employed by franchisors to monitor the performance of their franchisees in *newly-entered* and *distant* markets with special focus on the role of information exchange. Hypotheses relating franchisees' willingness to provide information to their respective franchisors are proposed. Specifically, it is suggested that franchisees' willingness to provide information to franchisors will be positively related to (1) the incidence of repeat purchases, (2) the age of the franchise relationship, and (3) the level of competition confronting the franchisees. In addition, multi-unit franchisees are expected to be more willing to provide information to their franchisors than their single-unit counterparts.