**MGT 403**

**ENTREPRENEURSHIP**

**LECTURE 18**

**Handouts Lecture 18**

**Franchising:**

**Definition:** A system in which semi-independent business owners (franchisees) pay fees and royalties to a parent company (franchiser) in return for the right to become identified with its trademark, to sell its products or services, and often to use its business format and system.

**Parties in franchising**: Two major parties contribute in franchising i.e. Franchisee and franchiser, Franchisee is taker and franchiser is giver in franchising, franchisee makes agreement with franchiser to utilize/sell the services, products or utilize trade mark or/and business format of franchiser against the agreed fee and royalties.

**Franchising fee & Royalty**: Fee is usually paid at the time of start of franchising and while royalty is to be paid by franchisee to franchiser on regular basis according to decided intervals and percentages. Franchising is mostly adapted in case of well-known running businesses or renowned trademarks.

**Why and how of franchising**: Besides the agreement to utilize the decided elements of franchiser’s business franchisee is mostly paying for the experiences of franchiser. Before going into the franchising option the franchisee must be aware of what and why of the franchising e.g. If this franchise will be contributing in business goals that can’t be done without franchising option etc. While franchiser’s end its extra advantage because already franchiser is running a successful business / product. Franchising is generally an extra advantage for franchisers.

**Benefits of franchising:**

**Training and sharing experiences: I**n most of the cases the entrepreneurs don’t have experiences to run a successful business, in that kind of situation franchising is best option as franchiser usually share it experiences to franchisee through trainings and workshops classes etc. Not only these experiences are for start even franchisee can be provided with training of new products vice versa.

**Brand name:** Brand name is one of the biggest benefit of franchising, franchisee don’t have to create brand worth it is inherited by the agreement of franchising as in most of the cases brand name is legal to be cloned.

**Standardized product/ service:** business format is another benefit of franchising. Franchisee must take care of franchise and quality of service and products, franchiser ensures it through the quality audits and other techniques.

**Advertising & marketing**: Advertising/ Marketing is one of the considerable aspects of businesses in case of franchising advertising is mostly managed by franchiser or parent company, franchisee is not spending on advertisement/ marketing.

**Financial support:** In some cases, franchising agreement cater for financial support as well, franchiser can offer financial assistance through various kind of agreements like e.g. while offering financial support franchiser can impose the extra high rate of royalty etc. In some cases, franchisers have subsidiary financial support companies to support franchising via loans, packages etc.

**Proven product**: In franchising products are proven, franchisee don’t have to work on business lines of product quality or acceptance in customer circles.

**Business location**: Site location another inherited benefit of franchising, franchiser is helping hand itself in selecting the appropriate place for business because of its own product quality and success also in most of the cases franchiser keeps the site of franchisee safe via the territorial encroachment protection agreement.

**Business success:** There are more chances of business success as compared to the independent entrepreneurship, franchising can offer the proven business experiences, publicly accepted quality products and business formats, well known trademarks and other above-mentioned benefits including, site selection, financial benefits etc.

**Drawback of franchising:**

**High fee and royalty**: Drawback of franchising is high rate of fee and royalty, **Adherence to product services**: strict adherence to the products and services e.g. in food product franchisee can’t even alter the recipe without the consent of franchiser.

**Purchase restrictions:** Franchiser can impose restrictions on purchasing i.e. franchisee must buy raw material or components of product from the franchiser approved supplier despite the franchisee known suppliers with lower rates of raw material etc. Purchasing restriction on franchisee can limit from lot of financial benefits, products alteration, innovation etc.

**Limited product line**: Limited product/ service line can be the other drawback of franchising, **contract renewals:** and terms can be a draw back because its mostly dependent on franchiser i.e. extension, retention or termination of agreements/ contracts.

**Unsatisfactory training program**: Besides supporting training programs, they can prove to unsatisfactory as well it depends on the agreed model by both franchisee and franchiser. **Market saturation:** Market saturation is another drawback for the franchising, likewise other business models market saturation can adversely affect the franchises etc.

**Factors making franchising appealing:**

**Marketing advertising:** Franchising has unique concept of marketing as explained earlier marketing and advertising are mostly managed by experienced franchiser.

**Profitability:** Profitability registered trademark, training programs, business system at work, affordability are the factors that are making the franchising appealing to the entrepreneurs and in some cases business person with prior business knowledge adapting it for the mentioned reasons.

**Trends shaping franchising:**

**Multiple unit franchising**: In multiple-unit franchising is trending, in that cases more than one franchises can be owned by same franchisee of same franchiser but at different locations. **International franchising:** International franchising is another trend shaping franchising, because of standardization and ease of replication franchising makes it easy to go international however in other models it’s not much easy to go international.

**Not traditional business sites**: Other trend is franchises are offered at nontraditional laces like, resorts, railway and buss stations etc. before that trend franchises were offered only at major city centers etc.

**Conversion franchising**: Conversion franchising is another shaping trend already established business can do franchising with the established franchiser/ well know companies to adopt their business model/ business format etc.

**Master franchising:** Master franchising is another franchising trend in which the initial franchisee is become master and for further franchises of same company in defined territory the master franchisee acts as franchiser of new or upcoming franchisees. Master franchising is authorized through the first franchiser or original owner of company / product.

**Piggybacking:** Piggybacking is trend in franchising that can be utilized to share the same franchise for two different companies or franchisers the fees and royalties are decided for each part and percentages are decided according to agreed business models.

**Ten Myths of Franchising:**

**1. Franchising is the safest way to go into business because franchises never fail.**

While brand recognition, location, and a developed business system can take you far, the benefits of franchising do not automatically guarantee you success. Franchisors promise to offer the tools to succeed, not guaranteed success, and if they do, that is something to be very leery of. Owning a franchise is hard work and the only person responsible for the success of your business is you.

**2. I’ll be able to open my franchise for less money than the franchiser estimates.**

One of the great things about franchising is that it is suitable for every budget. Many franchises can be started for less investment and some can be started for more. Other than the one-time, upfront franchise fee and royalties, the expenses would not be different from most other businesses. Franchising investments can be fitted to your own budget, but remember, those costs may come with several benefits that a start-up would not.

**3. The bigger the franchise organization, the more successful I’ll be.**

Branding can work for or against you – if the national brand has success, you will draw in more people but if the brand is flailing or has experienced a public relations fiasco, your business will feel the pain. As novice entrepreneurs, it is easy to believe that a strong brand will equate to a successful business but people are not as brand loyal as we may think they are. The brand should not be at the top of your list when searching for a franchise – things like ROI, success rates, structure, product quality, and initial investment should be.

**4. I’ll use 80 percent of the franchiser’s business system, but I’ll improve upon it by substituting my experience and know-how.**

Franchisors want their franchisees to be successful! Without successful franchisees, there would be no franchise and they would not be able to collect royalties. Unsuccessful franchises damage the brand and deter potential franchisees from seeking opportunities. It is in the best interest of the franchisor to help their franchisees run a successful business.

**5. All franchises are the same.**

Franchisees are small business owners who have invested in and support their local communities, even though their franchise system may be national or international in scope.

**6. I don’t have to be a hands-on manager. I can be an absentee owner and still be very successful. . I don’t have to be a hands-on manager. I can be an absentee owner and still be very successful.**

Wrong again. Franchises are not the type of business you can invest in and then sit back and collect a paycheck. If that was true, the franchisor would have no use for the franchisee. While some franchises do offer an absentee option, most are going to require at least some work on your part. As the owner and key investor, you have a vested interest in the success of this business and thus it would behoove you to be actively engaged.

**7. Anyone can be a satisfied, successful franchise owner.**

**8. Franchising is the cheapest way to get into business for yourself**

The beauty of franchising is that it offers opportunities in every industry and comes with a plan designed for success! This is a great opportunity to pursue a career in a field of your choosing where you will receive training, ongoing support, marketing materials, products, and a business plan from a tried-and-true corporate partner.

**9. The franchiser will solve my business problems for me; after all, that’s why I pay an ongoing royalty fee.**

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**10. Once I open my franchise, I’ll be able to run things the way *I* want to.**

**Detecting Dishonest Franchisers:**

* Claims that the contract is “standard; no need to read it.”
* Failure to provide a copy of the required disclosure documents.
* Marginally successful prototype or no prototype.
* Poorly prepared operations manual.
* Promises of future earnings with no documentation.
* High franchisee turnover or termination rate.
* Unusual amount of litigation by franchisees.
* Attempts to discourage your attorney from evaluating the contract before signing it.
* No written documentation.
* A high pressure sale.
* Claims to be exempt from federal disclosure laws.
* “Get rich quick” schemes, promising huge profits with minimal effort.
* Reluctance to provide a list of existing franchisees.
* Evasive, vague answers to your questions.