

THE ROLE OF FRANCHISING IN ENTREPRENEURIAL ACTIVITY

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ABSTRACT: *The franchise has been known in many countries as a means for successful business development, already occupying an important place in the developed market economies. Regarding the franchise as a real "engine" for the development of the SME sector and as an important external development tool we thought it appropriate to highlight a number of specific aspects of the franchise business.*

KEY WORDS: *franchise, business development, SMEs, entrepreneur, company.*

JEL CLASSIFICATIONS: *M21, M13.*

1. THE FRANCHISE – CONCEPT

Franchise means a system through which an entrepreneur, the franchisor, transmits its own savoir-faire to other entrepreneurs, the franchisees, thus controlling its correct implementation, in exchange for a financial contribution. This concept must be reproduced easily in multiple places.

The franchisor is an operator that: owns the trade mark; offers a set of products and/or services and/or technology; provides initial training for the exploitation of the registered trademark; uses its personnel and financial resources to promote the brand, for research and innovation, ensuring development and reliability of the product.

The franchisor is usually a well-known company, a producer who has goodwill and a notorious registered trademark which attracts consumers. This mark or symbol must be protected at least for the duration of the contract. It invests in human and financial assets for the promotion of the trade mark, and to ensure the success of the concept.

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The franchisee is a natural or legal entity, approved by the franchisor, which adheres to the principle of uniformity of the franchise network, as it is defined by the franchisor.

The franchisee invests capital, time, labour, commercial experience from the past in order for the new system to operate successfully.

Franchising is a chain of small businesses linked through image and policies of the parent company. The person who buys a franchise does not buy a company. He buys a "success package" from a company that shows him how to use it (McIntosh, 1985).

As regards the *types of franchising*, contracts can classify into three main categories according to the object of the main activity (Cocriș & Ișan, 1995):

A product distribution franchise licenses the franchisee to sell specific products under the manufacturer's brand name and registered trademark through a selective, limited distribution network.

Trade name franchise involves a registered brand name such as Pizza Hut or McDonald's. Here, the franchisee purchases the right to become identified with the franchisor's trade name without distributing particular products exclusively under the manufacturer's name.

A pure franchise - provides the franchisee with a complete business format, including a license for a trade name, the products or services to be sold, the physical plant (buildings, equipment), the methods of operation, a marketing strategy plan, a quality control process, a two-day communications system and the necessary business services. The franchisee purchases the right to use all the elements of a fully integrated business operation.

2. ADVANTAGES AND DISADVANTAGES OF FRANCHISING

In a market economy, franchise as a method of investing has been continuously strengthened, and its use is becoming more widespread as a result of certain factors, among which the most important are:

- renewing entrepreneurship, which causes many individuals to engage in business and for most of them, franchising is the best alternative;
- demographic factors and changing lifestyles, due to the increase in the number of families in which both spouses have a job, have exerted tremendous pressure on the demand for services and at the same time they provided an opportunity for cost effectiveness and for quick and quality services - two of the specialties of franchising;
- increasing the number of active women and of those who resigned or were dismissed from big companies, the majority wanting independence of action.

Among the advantages this business offers the franchisor, it's worth mentioning the following:

- franchising is a relatively quick way of expanding a distribution system with a minimum of capital;

- the ability to expand without expenses generated by finding and training managers. Obviously, the franchiser has to assess the quality of potential entrepreneurs and to identify those who do not possess appropriate qualifications, but generally, the task is much simpler than the one implied by developing the business on his own;
- franchisers earn percentages of the turnover, paid by the franchisees;
- a franchiser can grab a share of the regional or national market relatively quickly, without the need to invest a great amount of capital.

As regards the advantages conferred by the franchise to the franchisee, we can mention the following: standard quality products and services; managerial training; widely recognized brand names for products and services; national publicity and advertising programs; financial assistance; licensed products and business models, etc.

However, before deciding to jump at such a business, the entrepreneur needs to know, besides the advantages it offers, what are its limits or disadvantages.

These may take the following forms:

- the cost of franchise is often quite high for the possibilities of many entrepreneurs; it requires a strict adherence to standardized operations;
- in order to maintain quality standards, it is necessary for the franchisee to purchase prime or raw materials from approved suppliers, which places certain restrictions on purchases;
- the existence of restrictions as regards the marketing of other products.

Considering the fact that the franchise is an important tool in any market economy, in particular as regards external developments, in order to achieve success, it is necessary to take into account a number of issues such as:

- the franchiser must have rich experience, significant financial and time resources;
- a good cultural compatibility is needed between the object of the franchise agreement and the environment in which it is applied;
- it is important to conduct an intense and sustained promotion of the mark held by the franchisor on a new market.

However, despite the difficulties, the franchising agreement is extremely flexible, offering the possibility to adapt to the specific conditions in each country.

3. FRANCHISING IN ROMANIA

Franchise has been admitted in many countries as a successful method for business development. The franchise has won a reputation in Romania after many investors had used this method to set up safe and profitable businesses.

The history of franchising in Romania starts in 1975, when the first commercial agreement which contained specific franchise elements was signed. The contract was concluded by HERTZ and Automobil Club Român. The first classic franchise on the Romanian market is "McDonald's" which opened a franchise unit in 1995.

In early 2002, in Romania there were about 30 franchise chains. Companies such as McDonald's, Coca-Cola, Shell and Fornetti were able to develop successful

systems on the Romanian market. The failure rate of these businesses was almost zero and the operators were enjoying the benefits of the system (www.wikipedia.org).

The business environment becomes more favorable to franchises in 2006 when the Romanian Franchise Association is set up. The Association promotes the franchise as a business method on the Romanian market and initiates actions against illegal franchises and businesses, as well as in order to combat theft of know-how.

In 2007 the franchise system brings a new advantage to franchisees. As a result of the accession of Romania to the European Union, all companies must comply with EU regulations. In 2007 the best franchise brand was Fornetti with 400 units open.

The first attempt of a local brand to enter the market from outside Romania, through the franchise system, took place in 2008 when Jolidon exhibited its products for the first time at the Franchises Salon in Paris.

Currently, **the franchise business market in Romania amounts to about 1.4 billion euros annually**, as it is shown in a study carried out by KeysFin Company. Over 500 franchise companies are currently operating in Romania and their annual turnover is estimated at 1.4 billion euros, the most successful 'turnkey' businesses being those in the area of fast food and services, according to experts from the business information and credit management KeysFin Company.

In 2013, the value of franchise market stood at about 1.3 billion euros, while this year it is estimated an increase of 100 million euros amid estimations of consumption recovery, in the second half of the year.

According to estimates by Eugen Driga, senior consultant at IMO Group, in the year 2013 Romanian entrepreneurs have invested capital into fast food businesses (23.3%), coffee & restaurants (6.2%), retail businesses (26.4%), beauty, car service, real estate, furniture, services (28.8%) and hotels (2.3%).

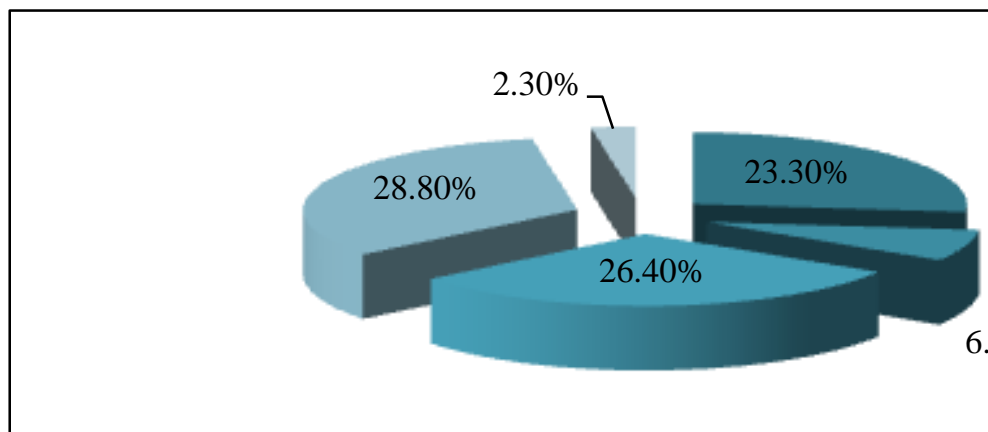


Figure 1. Investments in franchise businesses, according to fields of activity, in 2013

At the present time, there are many companies that, in the past, would allocate huge sums to expand on the Romanian market but in the long run they froze their budgets and chose the franchise. Such firms seek businessmen willing to pay for a turnkey business in which both parties have something to gain.

Metro with 'La doi pași', Elvila, Romstal, Carrefour, Subway, Crowne Plaza, Howard Johnson, etc. are some of the companies which have developed such concepts in recent years.

In Romania, where until recently the most quoted franchise fields were retail and food & beverage, in the past two years, franchises which have as field of activity education and human resources have also entered the market. At present, an important growth of franchises has been registered in the sector of education, from nursery schools to training services.

It is noticeable, however, that in our country most franchises are in the fast-food sector. There are hundreds of operators, most of them in the pastry industry. I think that the fast-food business is going great because it combines three important elements - price, quality and time spent to have meals.

Another segment which registers very good results on the franchise market of Romania is that of gambling and betting activities. Their success is due to the illusion of overnight gains, amplified by the economic crisis. Edifying examples in this respect are the betting shops StanleyBet and PublicBet.

However, one must keep in mind that many of the franchises do not conform to the current economic situation, because they require major investments or determine sales costs the way too high for the Romanians' purchasing power. Thus, the greatest degree of risk, at present, can be found in the real estate and in financial advice sectors. Centralized statistical data provided by KeysFin, show that, out of the 12,000 active real estate agents operating before the crisis, about 9,000 ceased their activity. Among the affected franchises, one may find Re/Max, Century21 and Hirsh.

Considering the franchise as a real "engine" for the development of the SME sector, the approach of specialists from the Rentrop Straton Market Research to investigate the level of knowledge, the degree of interest and the Romanian entrepreneurs' perception about the franchise business seemed appropriate to us. The company mentioned above conducted a research in 2011, on a sample of 894 respondents involved in the management activities of companies in Romania. The conclusions arising from this study are interesting and they give us an insight into the attractiveness of franchising in our country.

At the present time, it is relevant that the majority of respondents (58.7%) prefer the services sector when starting up a business. Activities that are considered the most promising are related to financial services, accounting, and consultancy, services in tourism, education, information technology and communications. Significant percentages correspond to managers who are drawn to the retail industry (10.8%), fast food (9.1%) and coffee shops (9%) (<http://issuu.com/think.big/docs/top100francize>).

As regards the interest in investing in franchises, the vast majority of respondents (79.7%) seem very interested in investing in a franchise business, while 14.9% have gone beyond this threshold of pure theory and created a project in this area / started up a business in this area (<http://issuu.com/think.big/docs/top100francize>).

The figure 3 reveals a low proportion of managers who are not interested in any kind of investments in franchises (5.3%).

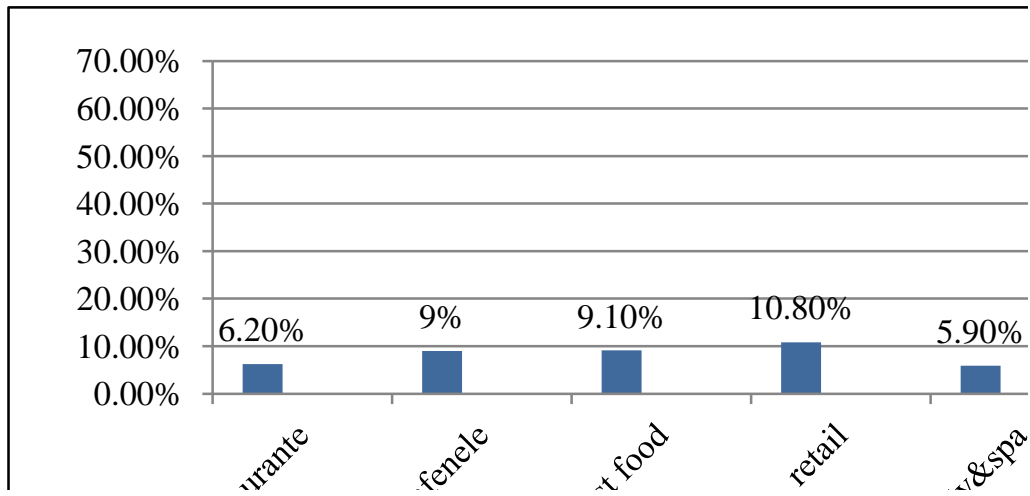


Figure 2. Preferred fields of activity on business startup

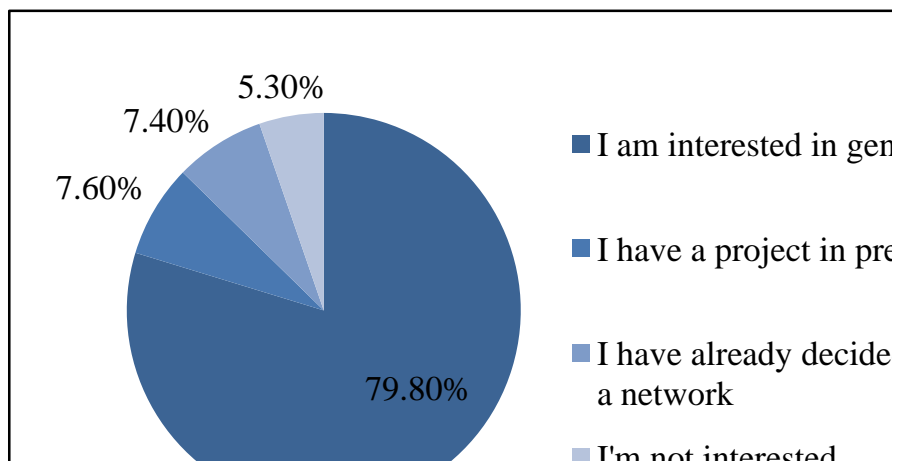


Figure 3. Level of interest to invest in a franchise business

From the perspective of the persons interviewed, **the most appreciated advantage of the franchise lies in the notoriety of the franchise brand** (17.1%). Other advantages with almost similar shares, identified by respondents are (<http://issuu.com/think.big/docs/top100francize>):

- the support received (14.8%);
- the range of products, services and available technology (13.7%);
- quick startup (12.8%);
- the power of the chain (12.8%);
- publicity of the group (12%);
- logistics (12%).

The less known advantage of the franchise is adapted training (5.2% of respondents).

As for **the risk associated with franchise**, the percentage of those who consider franchise as risky in a small or very small degree (18.6%) exceeds the cumulative percentage of those who, at the opposite pole, believe investments in franchises are risky in a large and very large degree (16%), which can reveal a certain "optimism" of potential investors regarding their expectations related to the future of the business.

The "optimism" of managers in relation to the estimation of the risk degree of an investment in a franchise is not lacking in realism. This remark grew out of the respondents' answers regarding the risks associated with this type of business.

Thus, the main risk is attributed to costs (38% of respondents), closely followed by the limited development of the business (36.2%). Moreover, the loss of independence is considered a risk by 23.8% of respondents (<http://issuu.com/think.big/docs/top100francize>).

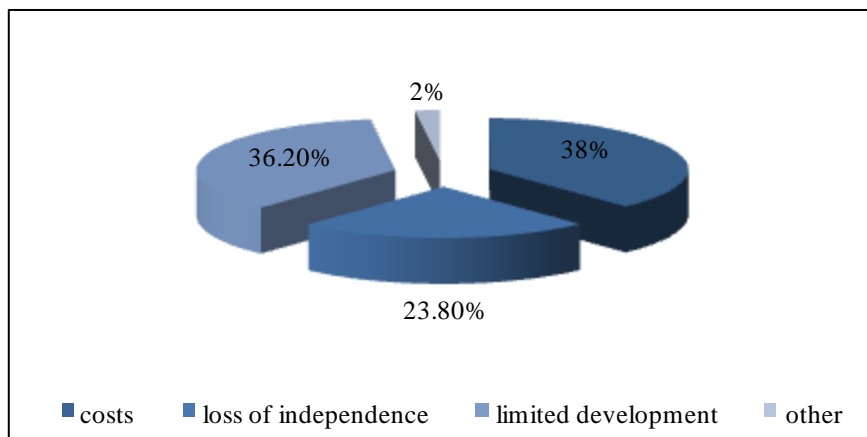


Figure 4. Types of risks associated with franchise

Other risks mentioned by those interviewed are: failure to adapt to the local market, limited flexibility, insufficient support from the franchisor, and also some risks associated with any business in general, as well as the wrong location, competition, the incompetence of the entrepreneur or the economic crisis, reflected, among others, by the decreasing purchasing power of the population.

4. CONCLUSIONS

The franchise has been appreciated in many countries as a way to success for business development. The franchise has won a reputation in Romania after many investors have used this method to set up safe and profitable businesses.

The prosperity of the sector entails the existence of financial and human resources necessary for the franchise, the existence of an infrastructure and initiative specific to a healthy economy.

Franchise has a catalyst role in a competitive market economy. If small businesses are the basis of franchise development, franchise in its turn can contribute to strengthening the small business sector, in particular and the economy, in general. Therefore, the interest is common, and the support is mutual. The prosperity of small and medium size enterprises facilitates the development of the franchise, while the franchise gives solutions to some problems and shortcomings of local entrepreneurs or enterprises.

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