

# Characteristics and types of franchises



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## Franchising

It is an agreement between two parties; one is the franchiser and another franchisee. The franchiser grants the right to franchisee to exploit its trademarks and trade names as well as other business to produce and market commodities, goods, or services in compliance with specific standards and requirements. The franchisee usually has to pay one-time franchise fee plus in addition some specified percentage of sales return as royalty. Other advantage includes immediate name recognition, standard design and decor, tried and tested products, promotion of business, training of employees, tried and tested products and up gradation of products. The franchiser gains fast expansion of earnings and business at minimum capital outlay.

One of the important characteristics of the franchise is that every purchaser undertakes a duty to fulfil the various conditions and requirements of the franchiser (seller) that are related to production and sale of goods and services to its customers. Under the agreement, the franchisor is obliged to provide advice on location of corporation, advice on management, helps in training and development, selection of equipment and may also provide financial assistance. All the above encourages the unification and standardization of services and products of the companies including the provision of unity on market design and style, events, the quality of services and goods and the additional benefit to the franchisor.

Some of the advantages of franchising mode (Kotler, 2002, p. 377):

1. Lower level of capital investment.

2. Reduction of personnel costs of the vertically integrated network management.
3. Expansion of sales market with the increase in sales volume and territory expansion.
4. Helps to build the prestige and goodwill of the company and its trademark, recognition, increased quality of goods and range of products of the company.
5. Increase in income from sale of the license, renting real estate franchise equipment.
6. Reduction in time of turnover.

Some of the disadvantages of franchising mode (Kotler, 2002, p377):

1. Difficult to control the reliability of financial reporting franchisee.
2. The franchisor may be made out of franchisee company a possible competitor
3. Low and poor reputation of the franchises may affect the quality control of the firm.

### Joint Ventures

It is an arrangement in which two or more parties team up to pool their resources, share control and ownership over the company's activities to achieve the common goal. They are often created to access the foreign markets which are otherwise very difficult to access directly. There are many well-known associations of firms that come together to get competitive advantage and penetrate new markets in form of joint ventures.

The following are the reasons why joint ventures can be the privileged method of admission to the foreign markets. The reasons are as follows:

1. Lack of managerial, financial and technological expertise for self-development in foreign markets.
2. In the case where government does not admit and allow access to foreign firm or subsidiaries to the local market without the participation of local capital for political and economic reasons.
3. Due to economic reasons, the company may team up with foreign firm for joint sale and production that will provide higher profits due to low cost of local labour, raw materials, etc.

Some of the drawbacks of joint venture strategy as entry mode to foreign markets are (Kotler, 2002, p. 377):

1. Conflicts and contradictions between the parties who form the joint venture can be related to different viewpoints on the use of profits and its allocation, management activities and implementation of different investment and financial strategies.
2. The need in strong partnership in the financing and creating of the joint venture can impede the realization of the company's transnational production and marketing policies.

#### Foreign direct investment

It is the most complete form of involvement in foreign market in the form of capital investment by creating own production plants and assembly centres.

FDI's are defined by so called the concept of control in which the main idea it to have major control and influence on management decisions. Even though

there is no full 100% ownership interest; a small percentage or higher shares may have effective control over companies' decision making and policy formation (Kotler, 2002, p. 378):

However several advantages of foreign direct investment mode include (Kotler, 2002, p. 378):

1. All the profits earned from investments belong to the company with full control on capital allocation further which can be used for long term production and marketing strategies.
2. Creating employment opportunities for the local market as well as tax payment can make a favourable image in the eyes of local government and its population.
3. The company can book profits with the help of cheap local raw materials, labour, saving transportation costs, expenses, etc. which can be used further for effective marketing activities and expansion of sales activities.
4. The company can adapt to the new environment for its products, services and marketing strategies by maintaining close and favourable relations with distributors, suppliers, agents, legal advisors and customers of the company.

Direct investment capital is carried principally in two forms; the export of loan capital and venture capital.

Venture capital is generally brought in international market in the form of direct investment and portfolio investment. Direct investment includes total control and acquisition of local company's stake. Whereas portfolio

investment includes buying stocks of foreign companies overtaking control over its can provide investors with high gains. Loan capital is the loans provided by state agencies and governments, companies, etc. which is divided into short term loan usually up to two years and long term which is over two years of time period (Kotler, 2002, p. 378).

### Turnkey projects

Another example of the commonly used foreign entry mode is a turnkey project. It is presented in the form of contract between two parties, according to which one party agrees completely construct, design and supply with equipment business/plant/service facilities and give the fully finished project to another party for agreed upon remuneration. Turnkey project generally used by the producers of industrial equipment and often provide predesigned project with required equipment. In majority of cases turnkey project requires complicity of construction companies; however, it can be substituted by equipment producer or consulting company, in the situation when company is not capable to find suitable object for investment abroad.

Turnkey project's main advantage lays in opportunity to generate significant income and spread there activates abroad by construct own buildings, plants, or manufacture, particularly, in the areas with limited access to foreign direct investment and with absence of professional expertise.

One of main disadvantages of turnkey project as a mode of entry into foreign market is a time, what can be explained by the risk of disclosure secrets of company to rivals father leading to hostile overtake of company's factories and plants. The same problem can arise in the case . Even though, many

companies interesting in establishing their facilities, especially if the host country has limited foreign ownership (Subba Rao, 2010).