



## Rosenberg Center Study Confirms Global Franchise Growth

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The Rosenberg International Center of Franchising has been working with the International Franchise Association Educational Foundation and the association's Global Marketing Committee on a research project that investigates the current state and expansion plans of U.S.-based franchisors in international markets. This research focuses on specific overseas regions, the first being the European Union. In addition, the researchers are working with members of the GLOMAK Committee to develop an International Franchise Risk Assessment Model that will help franchisors to evaluate the potential risks involved in expanding into foreign markets. The model takes into consideration local cultural, political, legal and economic country risk factors that could impact entry or expansion of a franchise system into an overseas market. In addition, competitive, demand and operational factors will be assessed.

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The first phase of the research findings were presented to the Educational Foundation and the GLOMAK Committee at the IFA's 46th Annual Convention in Palm Springs. The UNH researchers surveyed 104 U.S.-based franchise companies, representing more than 115,000 units worldwide. The findings focused on the general growth of franchising globally, comparing results from the 1989 Walker and the 1996 Arthur Anderson studies. In addition, the research investigated franchisor expansion strategies by region, preferred ownership types, and the strategies that are currently employed for international expansion. The research findings on the European Union will be published in an upcoming edition of Franchising World.

### Online Survey Sample

The 104 franchise systems that responded to the online survey were comprised of 11 primary categories. About half of the respondents were from the quick service restaurant sector (20 percent), retail products and services (14 percent) and commercial and residential services (13 percent).

### Current Overseas Presence and Profitability

More than half of the U.S.-based franchise companies (52 percent) surveyed currently operate units outside the United States with almost one-third of their total franchise units being operated overseas (30.2 percent). This is nearly a 20 percent increase in international expansion of U.S.-based franchise systems since 1996, and a 53 percent increase since 1989.

The preferred areas for overseas expansion in the past have been Europe (8.4 percent) and the Pacific Rim countries (8.3 percent), followed by Canada (5.2 percent), South America (2.6 percent), China/Macau/Hong Kong (2.3 percent), Middle East/Africa (1.8 percent), Mexico (1.3 percent) and Russia (0.1 percent).

Of the companies surveyed, 17.4 percent of their total profit (EBITDA) was generated from non-U.S. operations.

### Poised For Expansion

Those surveyed appear poised for expansion. Nearly four-out-of-five franchise companies (79 percent) plan to open new units outside the United States in the next three years, which represents a 44 percent increase since 1996, and nearly a 70 percent increase since 1989. Canada (26 percent) and Europe (15 percent) were the primary areas targeted for overseas' expansion during the next three years. Pacific Rim countries (9 percent) and China (7 percent) also emerged as strong contenders.

The survey shows that expansion into China is growing, led by the lodging and quick-service food sectors. With a population of more than 1.3 billion, China is expected to continue to attract the attention of U.S.-based franchisors.

### Overseas Expansion Strategies

Franchisors employ a variety of strategies to foster international expansion. However, only one-out-of-five companies surveyed have a corporate development plan for overseas expansion in place (21 percent), and only about one-out-of-five have an inhouse corporate position in charge of international development (18 percent). Given the importance that franchisors attach to international expansion, these findings are surprising. International expansion is complex and requires a thorough

understanding of foreign markets in terms of culture, legal, tax and supply chain issues. Not establishing a well-defined strategic plan and putting into place an organizational structure with the appropriate competencies to implement such a plan increases the risk in an already challenging environment.

Furthermore, the research indicates that only about 10 percent of franchisors participate in overseas trade exhibits and trade missions. This finding seems to indicate that either these venues are seen to be of low value by franchisors or their value is not well-understood or communicated. In addition, the use of lawyers and consultants specializing in overseas franchise system development support is low, with only about 15 percent of franchisors employing such services.

In open-ended, one-on-one interviews with executive level franchisors, researchers learned that problems are often averted when a well-researched corporate expansion strategy is in place. Unfortunately, in too many instances this has not been the case. Several franchisors indicated that they had entered foreign markets without having conducted a thorough due-diligence process.

#### **Difficulties Encountered**

Some of the most commonly cited problems occurred in the following areas:

- The joint-venture partner was unreliable or unable to implement the business plan.
- The labor laws of the local country were inflexible and there was a high level of bureaucracy that stifled growth and profitability.
- The unexpectedly high cost of site development and or leases.
- Difficulty in finding appropriate sites.
- Ineffective local supply chains and infrastructure.
- Difficulty in understanding and assimilating the local culture.
- Entrance into markets at the wrong time (i.e. political and or social instability, regulatory constraints, foreign ownership restrictions).
- Legal problems regarding intellectual property rights (patent and trade mark protection issues).
- Locations were too dispersed to allow for adequate and cost-effective supervision.

#### **Successful International Experience**

Franchise companies that experienced positive international results felt that their success was significantly enhanced by adequately researching the targeted foreign area, establishing a pilot unit, and using a “hub and spoke” expansion strategy in a given region. One franchisor stated that being able to adjust its U.S. system to the local culture in terms of product and service delivery was a key factor in their success.

#### **Looking to the Future**

The existence of a vibrant global economy is an established fact, but it is not an arena without risk. The results of this research indicate that U.S.-based franchisors have been on the forefront in expanding their systems internationally and that effective international expansion strategies will be a key factor in the achievement of successful growth and profitability. The challenge that franchisors face is how to adequately assess the risk involved in international operations and how to effectively adjust to an ever-changing global environment. As John F. Kennedy stated, “Change is the law of life. And those who look only to the past and present are certain to miss the future.”

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