

FRANCHISING AS A GROWTH STRATEGY. EVIDENCE FROM ROMANIA

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Abstract: *There are many ways in which businesses can growth. Aim of this article is to make the business owner aware of the scope of the franchise and business opportunity law and how they may affect growth strategy tried to be employed by the business owner. For this purpose we present a list of advantages and disadvantages of franchising for the franchisee and for the franchisor and examined the status and trends of the Romanian market franchise, especially in clothing, which are available for prospective franchisees in Romania. We find out that although it is increasing its level of development is much lower than in EU, (according to Romanian Franchise Association in Romania are slightly over 400 franchises, with various business fields, while in the Europe there are about 10,000 franchise networks). Reasons for slower development of the textile franchise business in Romania can be found in the effects of economic crisis on the Romanian economy, which shifted the structure the consumer spending of the people of Romania, expenditures for clothing and footwear have decreased and have reached at 5.3% of total household expenditure. In these conditions, the clothing franchises who had suffered most in Romania were those whose offer to address at high-income consumers (Escada, Esprit, Etam) and medium (Debenhams, Gap). Less affected were franchises for which targets are low-income consumers and who besides the low price of products offers a wide range of products and models with a very short life cycle (fast fashion). The information for this paper was gathered from literature, from the analysis financial indicators of the different companies and by Internet.*

Key words: *economic, development, franchisor, franchisees, brands*

1. FRANCHISING AS GROWTH STRATEGY

Franchising is being used as development and growth strategy in numerous contexts across the globe, ranging from its use as market entry to an expansion mode and a strategy to secure competitive advantage. [1] In the last decades, strategy of franchising has played a vital role in small and medium business development and has become an important growth option, so for many companies, franchising is a means of expanding business and for individual entrepreneurs, is a method of opening a business. Franchising is the fastest way to guarantee that entrepreneurs adhere to the high standards required for successful business management.

Because of the economic importance franchising has captured the attention of a wide range of researchers. From the perspective of entrepreneurship, franchising is a vehicle for entering business ownership [2], from the perspective of marketing, franchising is an important distribution channel [3], from the perspective of economics, franchising is a leading venue for understanding the structure of contracts [4] and from the perspective of strategic management, franchising is an important organizational form. [5]

Franchising is a business relationship in which the franchisor (the owner of the business providing the product or service) assigns to independent people (the franchisees) the right to market and distribute the franchisor's goods or service, and to use the business name for a fixed period of time. The International Franchise Association defines franchising as a "continuing relationship in

which the franchisor provides a licensed privilege to do business, plus assistance in organizing training, merchandising and management in return for a consideration from the franchisee".

2. ADVANTAGES AND DISADVANTAGES OF FRANCHISING FOR THE FRANCHISEE AND FOR THE FRANCHISOR

Franchise system is designed to work well for both the franchisor and the franchisee. Franchise agreement is a formal relationship between the franchisor and franchisee to work together to build mutually beneficial business operations.

The "commercial marriage" between franchisor and franchisee is ultimately a legal relationship, with the full obligations and responsibilities of both parties outlined in a highly detailed franchise agreement. This commercial contract varies in length and conditions from one system to the next, such that it would be almost impossible for any two franchise systems to have identical agreements. [6]

By nature of the relationship, the franchise agreement will be imbalanced in favor of the franchisor, as the franchisor must at all times remain in control over certain standards critical to the ongoing success of the business format.

Nevertheless the development of this system is due to the numerous business benefits not only for the franchisor but also for the franchisee. Franchising is an entrepreneurial activity that plays a crucial role in the creation of new jobs and economic development. [7] According to Bond & Bond franchisees have a 77% chance of survival after five years of operation compared with 8% for new independent business ventures. [8]

Also, Franchising is an important part of the economy and a central phenomenon in entrepreneurship. Michael S.C. recommend franchising as a method that entrepreneurs can use to assemble resources to create large chains rapidly, especially for entrepreneurs who can create big franchise chains. [9] In return, the franchisee pays an up-front fee and ongoing royalties to the chain operator. [10] The franchisee obtains from the chain operator the right to market goods or services under its brand name and to use its business practices. [11] From this collaboration creates economic value.

Menekse and Orkide Salar used the SWOT analysis to identify the advantages, disadvantages, threats and opportunities of franchising. [12] This is shown in table 1 below:

Table 1: SWOT analysis of franchising

Strengths	Weaknesses
<ul style="list-style-type: none"> • Brand Recognition • Lower Risks for Failure • Easy Setup • Ready Customer Portfolio • Easy to Find Financial Support 	<ul style="list-style-type: none"> • High Cost <ul style="list-style-type: none"> - Initial Cost - Ongoing Costs • Dependency • Strict Rules
Opportunities	Threats
<ul style="list-style-type: none"> • Entrepreneurs have chance to become their own boss • It offers some market opportunities like discovery and exploitation 	<ul style="list-style-type: none"> • Continuing growth of existing franchised competitors • Other new franchise competitors entering market place • The decline of branding in market • The publication of New Business Models

According to *The International Franchise Association (IFA)* franchise businesses are important to the overall economy, generation in USA more than \$800 billion in annual sales, representing 40.9% of all retail and franchised businesses create more than 170,000 new jobs each year. Today more than 8 Million people are employed by franchise businesses. Total franchise sales over 1 Trillion.

Growth franchises is indicated also by the data published by IFA that looks like 1 in 12 business establishments is a franchise, a new franchise opens every 8 minutes of every business day and there are approximately 1500 Franchisors and 550,000 Franchisees.

3. STATUS OF THE FRANCHISING SYSTEM IN ROMANIA

Franchising has grown rapidly in Europe in recent years, but the industry is largely unregulated. The European Union has not adopted a uniform franchise disclosure policy. Only six European countries including Romania, have adopted pre-sale disclosure obligations. They are France (1989), Spain (1996), Romania (1998), Italy (2004), Belgium (2005) and Sweden. In addition there are

a number of countries that have general "good faith" type laws that can give rise to franchise disclosure obligations ("Good Faith Laws"). These countries are Germany, Austria, Portugal and Lithuania. [13]

In Romania, the franchising is regulated by Law no. 79 April 1998. Regarding the Legal Status of Franchise under the Romanian law, a franchise is defined as a marketing system where the franchisor grants to the franchisee the right to operate or develop a business, product, technology or service. In addition to requiring minimum provisions of the franchise agreement and regulating the post-sale franchisor-franchisee relationship, the Romanian act requires certain pre-sale disclosures. Among these disclosures are:

- a) the financial terms of the proposed franchise agreement, including royalties to be paid and purchases the franchisee is obligated to make,
- b) a description of franchisor's gained and transferable experience,
- c) the franchisee's area of granted exclusivity,
- d) the duration of the agreement, and
- e) the terms of the agreement governing renewal, termination and assignment.

There is no requirement under Romanian law for the registration or filing of franchises with the government.

The first classic franchise appeared on Romania market is "McDonald's" which opened a unit franchise in 1995. Among the earliest companies that have entered the market in Romania in the franchise are Pepsi and Coca-Cola.

Because business expansion in the franchise system in Romania and to enforce standards of a favourable business environment as franchising, in early 2006, was established Romanian Franchise Association, a non-governmental, apolitical and non-lucrative. One of the goals of this organization is to identify and resolve specific problems of franchise, to promote franchise as a way business in the Romanian market and initiating action against illegal franchises, to combat counterfeiting and theft of know how.

According to Romanian Franchise Association in Romania are more than 438 franchises, with various business fields. Across Europe there are about 10,000 franchise networks, 4,000 in China, 2,200 in USA, 1200 in Japan and 1000 in Australia. Analysis of the 2633 franchise units active in Romania in mid 2012 highlighted the areas most popular franchises:

Table 2: Fields of activity with most franchises

Field of activity	Percentage of total units
Personal services	30.54%
Retail	28.29%
Fast food	25.07%
Services companies	6.57%
Interior Arrangements	2.66%
Clothing and Accessories	2.47%
Food	1.63%
Real Estate	1.06%
Construction	0.65%
Restaurants & Coffee shops	0.65%
Hotels	0.42%

In the field of clothing and accessories, there are over 100 companies that have opened franchises in Romania, companies dealing with the production and sale of clothing and accessories or just dealing with marketing of these products (which are predominant). These companies cover all segments of the fashion & beauty area: collections of classic, elegant and casual collections of underwear, sports outfits and various complementary accessories to eyewear, watches, perfumes and cosmetics for men, women and children.

A study by ThinkBig Franchise Consultants and supplement "Money & Business" revealed the most expensive luxury retail clothing franchise foreign presence in Romania. The top ranking franchise is Max Mara, a luxury brand in Italy, known for its haute couture. Landscaping costs are the 1000-1500 euro/sqm, plus the cost of the stock plus the costs of launching and others. Ranked II Escada is a brand of luxury clothing for women. Rankings continue with Zara, part of Inditex, one of

the largest retail groups in the clothing industry in the world. Zara products follow the newest trend in the fashion industry, its stores were opened in major shopping centers in Europe, America and Asia. Besides these firms is also found Hugo Boss, Marks & Spencer, United Colors of Benetton, Mexx, Morgan etc.

Is noteworthy that in this top are present companies which represents different segments of customers: from out couture and high fashion (Max Mara, Escada) that targets are high-income customers at fast fashion addressed to middle-income customers (Hugo Boss, Mexx) and small (M & S, Zara, Benetton).

On the Romanian market, besides these international brands can be found Romanian companies who make franchising business - Jolidon, MEXTON, ID Sarrieri, Tina R, etc.

The first Romanian company which is selling international franchise is Jolidon - since 2008. Currently it has its own network of 87 stores in Romania and distribution in over 60. [14] The company has opened 10 stores abroad in Budapest, 33 stores in Italy and 10 in France. Besides these shops Jolidon lingerie distribute articles in the United States, Canada, Africa and Japan. Cost of opening such a store are between 60,000 and 90,000 Euro. [15]

Mexton is a Romanian brand of casual and elegant clothes, founded in 1997. Currently has a network of over 45 stores in many cities: Bucharest, Pitesti, Ramnicu Valcea, Sibiu, Deva, Arad, Timisoara, Oradea, Targu Jiu, Targu Mures, Iasi, Craiova, Braila, Galati, Brasov, Cluj Napoca. The costs of a Mexton franchise is: franchises fee - 5000 Euro and 3% royalty, total investment is 30,000 Euro. [16]

I.D. Sarrieri was launched in 1992, as a company producing indoor clothing (homewear and nightwear) and since 2002 is one of the most popular brands of luxury underwear market. Created by Iulia Dobrin and his team, with over 500 employees, this firm manufacture underwear. Collection I.D. SARRIERI are now sold in the finest lingerie boutiques around the world, from Paris to New York from London to Tokyo, from Brussels to Shanghai.

TINA R brand, was founded in 1994, became one of the leading brands on the Romanian market pret-a-porter. This brand, Tina R, is well known by most girls in Romania and includes the area of clothing (jackets, trousers, skirts, blouses, shirts) and all the accessories genres (bags, shoes, scarves, gloves, hats). The first franchise Tina R was sold in 2006. Opening a franchised store TinaR requires an initial investment of 100,000 euros, the franchise fee is 0.

Theory says that amongst the best Businesses in during crisis are franchises and distribution.

An example in this sense is the Mexton company, who despite all the difficulties succeeds in the last years to increase considerably turnover and profit obtained, especially in the last year analysed.

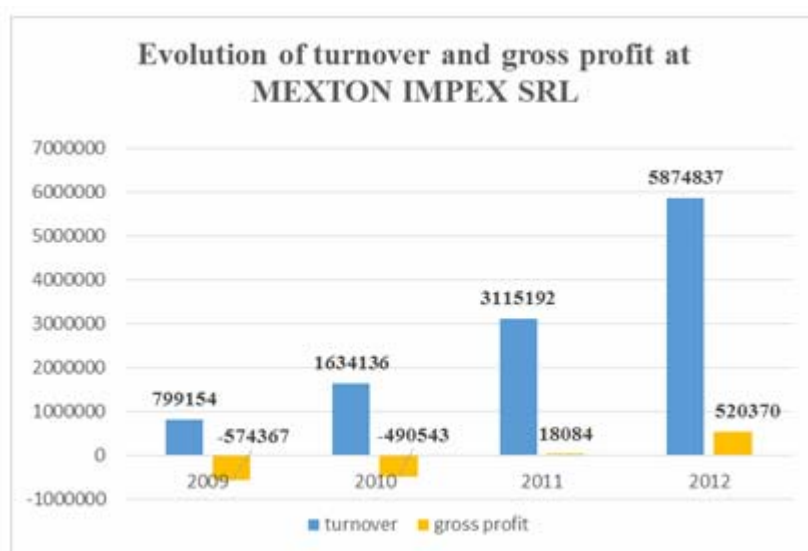


Fig. 1: Evolution of turnover and gross profit at MEXTON IMPEX SRL [17]

Reality highlights that not in all cases are recorded sustained success theory. For example companies Debenhams, Gap, Esprit, Etam, Celio, Mandarina Duck, Kipling, Olsen and Bally are some of the fashion brands that have permanently left Romania. [18, 19, 20]

Not only international companies have registered losses in this period of crisis but among Romanian companies. For example is entering in insolvency of the company Tina R Distribution, one of the companies in the group clothing retailer Tina R.

Reasons for slower development of the textile franchise business in Romania can be found in the effects of economic crisis on the Romanian economy in general, with its implications: reducing consumer purchasing power through the salary cuts that took place in the budgetary system, reduction or cancellation of various premiums or salary bonuses (spore of PhD, the XIII salary, various bonuses during granted the Easter holidays and Christmas holidays or other events), closure of many companies and therefore job losses for those employed in them.

All this have determined modification of consumption expenditures of the population in Romania. Main uses of the household expenditures in the second quarter of 2013, are the consumption of food, non-food, services and the public administration and the private and social insurance budgets in the form of taxes, contributions, fees, and expenses necessary household production. The expenses for clothing and footwear representing only 5.3% of the total. [21]

Another factor that determined the market exit of these brands has been developing extremely aggressive in recent years some brands extremely competitive as Zara, Massimo Dutti, Pull and Bear, Stradivarius, Bershka, H&M, which by offering very diverse and the prices charged were able to conquer larger market share at the expense of clothing products companies mentioned above.

In these conditions, the clothing franchises who had suffered most in Romania were those whose offer to address at high-income consumers (Escada, Esprit, Etam) and medium (Debenhams, Gap). Less affected were franchises for which targets are low-income consumers and who besides the low price of products offers a wide range of products and models with a very short life cycle (fast fashion). Besides these, an important contribution in maintaining these companies on the Romanian market have had the discounts awarded to loyal customers and the significant price discounts (up to 90%) when were changed the collections - these measures have contributed to increasing sales in the periods of their application.

4. CONCLUZION

The theory that the best Businesses in the time of crisis are franchises and distribution is not check completely. Reality has shown that it is not enough to have and promote a well known brand for to succeed on all markets.

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In these conditions, the clothing franchises who had suffered most in Romania were those whose offer to address at high-income consumers (Escada, Esprit, Etam) and medium (Debenhams, Gap). Less affected were franchises for which targets are low-income consumers and who besides the low price of products offers a wide range of products and models with a very short life cycle (fast fashion). Besides these, an important contribution in maintaining these companies on the Romanian market have had the discounts awarded to loyal customers and the significant price discounts (up to 90%) when were changed the collections - these measures have contributed to increasing sales in the periods of their application.

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