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Determining pros and cons of franchising by using swot analysis

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Abstract

This report is an attempt to compare the advantages and disadvantages of franchising which is one of the most known business model. To start with, the swot analysis is defined. Then, the advantages of Franchising are explained. These are brand recognition, low risk to failure, easy set up, ready customer portfolio and easy to find financial support. In the third part, the disadvantages of franchising are explained that are strict rules, dependency and high cost. Finally, in the last part, the advantages over disadvantages of franchising are analyzed and it is concluded that the franchising is more advantageous.

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Keywords: Franchising, swot analysis;

1. Introduction

Nowadays, business models are increasing. One of the most known business model is franchising. When there is an owner of national or regional chain company and a person who wants to operate one of their companies, they make a contract. This contract enables person to operate one of their outlets. These outlets must be same with the original company; using same furniture, equipment, having same service and taste. These contracts show differences according to the owners, it can be based on initial payment or a percentage of gross sales. To sign a contract in order to be a part of a known business is called as franchising. Franchising has been providing business opportunities for over 150 years.

"According to the International Franchise Association (IFA), the industry's largest trade groups, almost 4 percent of all small businesses are franchises and the industry accounts for 40 percent of all retail sales in the country" (Bohi, 2010, p.16). It is believed that franchising comes from the mid 1800s. The earliest franchising was done by Singer Sewing Machine in the United States in 1851. Coca-Cola started to franchise in 1899, then, oil refineries and auto manufacturers began to franchise to distribute their products in different parts of the country. After that, America wants to improve their restaurant chains and Kentucky Fried Chicken started in 1930, Dunkin Donuts started in 1950 and McDonalds which is the most successful franchise in the world started to franchise in 1955.

This paper has been written to determine the pros and cons of franchising by the help of SWOT analysis and compare them. This paper is divided into seven sections. The next section explains the literature review. The third section explains the SWOT analysis. The advantages are explained in section four. The disadvantages explained in section five. In section six, the advantages over disadvantages are explained. Finally, the conclusion is provided.

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2. Literature review

According to Franchise Facts 2011, today, franchising is big business, and there are over 3,000 franchise systems in the USA. Franchising is an entrepreneurial activity that plays a crucial role in the creation of new jobs and economic development (Falbe et al, 1998). In addition to this, Franchising is a prominent part of the economy and a central phenomenon in entrepreneurship. Practitioners often recommend franchising as a method that entrepreneurs can use to assemble resources to create large chains rapidly. (Michael, S. C, 2003). In addition to this, it is a method recommended especially for entrepreneurs who can create large chains with franchising. In return, the franchisee pays an up-front fee and ongoing royalties to the chain operator (Combs et al, 2004).

A franchise is an agreement granting a person or group of individuals (the franchisee) the right to market a product or service using the brand name and operating methods of a business (the franchisor) in exchange for a fee (typically an up-front fee plus recurring royalties on sales) (Knott, A. M., Corredoira, R., Kimberly, J., 2008). Moreover, Franchising has literally reshaped the retail landscape since its infancy in the 1950s. By most estimates, franchising now accounts for $1 trillion in annual retail sales from approximately 320,000 businesses in 75 industries and employs more than 8 million people (Dant, R. J., Kaufmann, P.J., 2003).

In franchising, a chain operator–entrepreneur collaborates with a franchisee–entrepreneur to create economic value. Specifically, the franchisee obtains from the chain operator the right to market goods or services under its brand name and to use its business practices (Barthelemy, J, 2011). In the global market, franchising adds value by enhancing the understandings of local culture, customs, and values (Contractor F. J., and Kundu, S. K., 1998).

According to IFA Educational Foundation, 2005, franchise businesses are important to the overall economy, generating over $1 trillion in annual sales—representing 17% of the U.S. Gross Domestic Product—and averaging 300 new franchise start-ups each year. There are approximately 901,093 franchisees and they are employing approximately 18 million people, in turn generating an economic output of over $2.1 trillion which equals about 40.9% of the U.S. retailing sector (Dant, R.P., Grünhagen, M. and Windsperger, J., 2011).

3. Swot analysis

SWOT analysis has its origins in the 1960s (Learned et al., 1965). In addition to this, The key tool used presently in planning the national sustainable development is Strengths, Weaknesses, Opportunities and Threat (SWOT) analysis, which originates from the business management literature and was adopted in the 1980s by public administration across such areas as regional development and municipal planning (Markovska, N., Taseska, V., and Pop-Jordanov, J., 2009). SWOT analysis is an important decision-making support tool, and is commonly used to systematically analyze the strategic situations and identify the level of organizations from their internal and external environments (Gao, C-Y., and Peng, D-H., 2011). Having identified these factors strategies are developed which may build on the strengths, eliminate the weaknesses, exploit the opportunities or counter the threats (Dyson, R. G., 2004).

This analysis helps organizations, projects or even individual about systematic thinking and comprehensive diagnosis of factors. In addition to this, the organizations can identify their positive and negative factors and then develop and adopt a strategy resulting in a good fit these factors (Gao, C-Y., and Peng, D-H., 2011). The strengths and weaknesses are identified by an internal appraisal of the organization and the opportunities and threats by an external appraisal (Dyson, R. G., 2004). The last version of SWOT analysis is developed by Dealtry in 1992. According to him, the steps are built on strengths, eliminate weaknesses, exploit opportunities and mitigate the effect of threats. The SWOT analysis is used to identify the advantages, disadvantages, threats and opportunities of franchising. This is shown in table 1 below.