

COMPILATION OF A PROFILE OF THE SUCCESSFUL FRANCHISOR IN THE SOUTH AFRICAN FRANCHISE INDUSTRY

I. DREYER Hons BA

Dissertation submitted in partial fulfillment of the requirements for the degree
Magister in Business Administration at the Potchefstroom Business School,
Potchefstroom Universiteit vir Christelike Hoër Onderwys.

Supervisor: Dr. A. M. Smit

November 2000
Potchefstroom

ACKNOWLEDGEMENT

Thank you to all franchisors, franchise directors and managers, for interviews granted and information shared.

Thank you also to Me Esmé Burger, and Mrs Marie-Lee du Plooy for their technical assistance as well as Dr. Anet Smit for her insight, and guidelines which kept this dissertation focused.

SUMMARY

The aim of this dissertation will be to compile a profile of the most important strategic management and leadership skills of the successful franchisor in the South African franchise industry. The role of the franchisor as entrepreneurial leader also plays an important role regarding the compilation of this profile. This will hopefully supply insight, guidelines and information to prospective franchisees as well as investors regarding “due diligence” – the process of doing the necessary homework before embarking on any franchise venture or engagement.

The first chapter of this dissertation is an explanation of the franchise concept, and also how, when and where it originated. It also supplies information regarding current problems and challenges facing the South African franchise industry. The advantages as well as the disadvantages for investing in such a venture is also discussed.

Chapter 2 discusses the many forms of franchising. It also supplies a formal definition of a franchise. Attention is drawn to the fact that notwithstanding a formalised agreement between franchisor and franchisee and a code of ethics written into such agreements, the franchise industry in South Africa is currently viewed with a lot of scepticism.

As stated in chapters 1 and 2, the main responsibility for the long-term success of a franchise concept lies with the *franchisor*. Chapter 3's aim is to determine through theoretical study and discussion not only the entrepreneurial mind of the franchisor in thought and action, but also the most important strategic management and leadership skills required to ensure long-term success.

Chapter 4 entails a field study by means of structured interviews, questionnaires and telephonic discussions with 10 successful franchisors to establish this profile. The chapter ends with an evaluation and summary, as

result, of the most important strategic management and leadership skills as identified by these 10 franchisors.

Chapter 5 finalise this dissertation with the conclusion that the successful franchisor, either as individual entrepreneur or experienced management team, indeed dispose of the required strategic management and leadership skills necessary to ensure the long-term success and growth of a concept. The successful franchisor assigns a high priority to deliverance of quality service, integrity, persistence, reliability, innovation and creativity. The successful franchisor also possesses above-average communication capabilities and have the necessary know-how and ability to attract the relevant skills and persons necessary to stay competitive and entrepreneurial. This profile of the successful franchisor, as well as additional recommendations given in this chapter, will hopefully provide guidance regarding the exercising of true franchise “due-dilligence”, specifically to investors wanting to invest in a franchise.

OPSOMMING

Die doelstelling van hierdie skripsie is om 'n profiel daar te stel van die belangrikste strategiese bestuurs- en leierskap vaardighede van die suksesvolle franchisor in die Suid-Afrikaanse franchise industrie. Hopelik sal dit insig, riglyne en addisionele inligting verskaf aan voornemende franchisees en beleggers, om sodoende deeglike navraag en ondersoek te doen voor enige franchise ooreenkoms aangegaan word.

Die eerste hoofstuk van hierdie skripsie verduidelik die franchise konsep; hoe, wanneer en waar die konsep sy oorsprong gehad het. Dit verskaf ook inligting rakende probleme en uitdagings wat die Suid-Afrikaanse franchise industrie huidig ondervind. Die voordele asook nadele ten opsigte van belegging in die industrie word ook bespreek.

In hoofstuk 2 word die verskeie vorme of tipes van franchising bespreek. 'n Formele definisie van 'n franchise word ook gegee. Dit word beklemtoon dat nieteenstaande die aanwesigheid van formele ooreenkomste tussen franchisor en franchisee, wat 'n kode van etiek insluit, verhoudings dikwels problematiek is. Dit is dan ook die vernaamste rede waarom dié industrie in Suid-Afrika huidig skepties bejeën word.

Soos beklemtoon in hoofstukke 1 en 2, is die langtermyn sukses van 'n franchise konsep die *franchisor* se verantwoordelikheid. Hoofstuk 3 is 'n teoretiese ondersoek en bespreking van die spesifieke entrepreneuriese vaardighede en aktiwiteite van die franchisor, asook die belangrikste strategiese bestuurs- en leierskap vaardighede wat benodig word om van die konsep 'n langtermyn sukses te maak.

Hoofstuk 4 is 'n veldstudie by wyse van gestruktureerde onderhoude, vraelyste en telefoniese gesprekke met 10 suksesvolle franchisors om hierdie profiel saam te stel. Die hoofstuk sluit af met 'n evaluasie van die belangrikste strategiese bestuurs- en leierskap vaardighede soos deur hierdie 10 franchisors geïdentifiseer.

Die skripsie word gefinaliseer in hoofstuk 5 met die afleiding dat die suksesvolle franchisor in die Suid Afrikaanse franchise industrie, hetsy individuele entrepreneur of ervare bestuursman, oor die nodige strategiese bestuurs- en leierskap vaardighede beskik om van die konsep 'n langtermyn sukses te maak. Die suksesvolle franchisor heg hoë prioriteit aan die lewering van kwaliteit diens, integriteit, betroubaarheid, volharding, kreatiwiteit en innovasie. Die suksesvolle franchisor besit n' bogemiddelde kommunikasie vermoë, en beskik ook oor die nodige kennis en initiatief om die relevante individue en vaardighede te bekom om sodoende kompetend en entrepreneurs te bly. Hopelik sal dit dan ook aan voornemende beleggers en franchisees riglyne en leiding verskaf sou die behoefte bestaan om te belê in die industrie.

TABLE OF CONTENTS

CHAPTER 1	FRANCHISING IN CONTEXT	1
1.1	Introduction	1
1.2	Background	2
1.2.1	The Franchise concept	2
1.2.2	Franchising in South Africa	4
1.2.3	The benefits/advantages and disadvantages of a franchise	5
1.3	Supposition	9
1.4	Aim of dissertation	10
1.5	Method of study	11
1.6	Progress of study	11
CHAPTER 2	THE SOUTH AFRICAN FRANCHISE INDUSTRY	13
2.1	Background	13
2.2	Formal definition of a franchise	18
2.3	The ethics of franchising	20
2.4	The franchisor and franchisee relationship	24
2.5	Problems and challenges facing the South African franchise industry	27
CHAPTER 3	SKILLS NECESSARY TO BE A SUCCESSFUL SOUTH AFRICAN FRANCHISOR	34
3.1	The franchisor as entrepreneurial leader	34
3.2	Leading practices of successful leading entrepreneurs	38
3.3	Common elements in successful intrapreneurship	42
3.4	The strategic management and leadership skills necessary to be a successful entrepreneurial franchisor	44
3.4.1	Developing a strategic vision and business mission	45
3.4.2	Setting objectives	46
3.4.3	Crafting a strategy	47
3.4.4	Implementing and executing the strategy	48
3.4.5	Evaluating performance, monitoring new developments, and initiating corrective adjustments	49
CHAPTER 4	FIELD STUDY AND RESULTS	51
4.1	Method of research	51
4.2	Respondents of research	51
4.3	Results of field study	52
4.3.1	The franchisor as entrepreneurial leader	52
4.3.2	Rating the importance of strategic management, leadership and administrative skills of the franchisor	54
4.3.3	Evaluation of results	57
CHAPTER 5	CONCLUSION	60
5.1	Exercising franchise "due-diligence".	60
5.2	The successful franchisor in the South African franchise industry	62

ANNEXURE A
ANNEXURE B
ANNEXURE C
ANNEXURE D

LIST OF EXHIBITS

Exhibit 2.1	Problems and challenges facing the South African franchise industry	27
Exhibit 2.2	The ethics of franchising	28
Exhibit 3.1	Model of the entrepreneurial process	36
Exhibit 3.2	The Entrepreneurial leader and team is the key ingredient for success	37
Exhibit 3.3	Who is the successful entrepreneur?	39
Exhibit 3.4	Common elements in successful intrapreneurship	43
Exhibit 3.5	Strategy is both proactive (intended) and reactive (adaptive)	48
Exhibit 4.1	Franchise business categories	52

CHAPTER 1

FRANCHISING IN CONTEXT

1.1 INTRODUCTION

“Own your own business!” “Be your own boss!” These kinds of headlines appear every day in business magazines, newspapers, classified advertisements and books. While these advertisements makes franchising sound appealing, they also may be misleading (Shephard, 1999: 33).

Many prospective franchisees mistakenly believe when they pay their franchise fee they are buying a business. Very frequently, the *franchisor* has not made the franchise relationship clear to these prospective franchisees, which results inadvertently in deciding to run things their own way, break the franchise rules and ultimately fail in the endeavour. More concerning and having a far-reaching effect on the franchise industry itself, is franchisors that use the industry as means of expanding an existing business due to lack of capital or take the route of trying to stay afloat financially by selling franchises (Venter, 1999: 18). The result is that funds that should have been used to build the franchise infrastructure never goes there and franchisees never receive the support that is their right. Inevitably the brand declines, franchisees are left in the cold and the company dies.

Currently a lot of “puffing” is the order of the day in the industry, meaning that franchising is marketed as the “alternative option” to gain financial independence and success, as well as seen as the cure for unemployment. However, not every concept is suited to franchising. Therefore franchisees who are also investors, run the risk of having to carry and market an idea or concept that are not viable or truly franchisable. Franchisors, mistakenly or unwillingly mislead by franchise developers and consultants, should for instance have been looking for agents, not franchisees (Anon, 2000: 24). A franchise

Used
Ch 1
=

business, unfortunately, cannot be build or grown on the strength of franchise fees alone. Combine this with a definite lack of strategic planning, management and leadership skills, and you have a recipe for failure. Failure which the industry cannot afford, and the very reason capital investors as well as the majority of financial institutions in South Africa is wary of investing in the industry.

The general aim of this dissertation will be to clarify “due-diligence”, the franchise relationship between the franchisor and franchisee in the franchise industry. The spesific aim will be to determine the entrepreneurial, strategic management and leadership skills in order to compile a profile of a successful franchisor in the South African franchise industry.

1.2 BACKGROUND

1.2.1 The franchise concept.

America has really fueled the explosive growth in franchising (Lipkin & Parker, 1999: 202). In America, franchising accounts for $\pm 42\%$ of all retail business and $\pm 10\%$ of the gross national product. In Australia, franchising accounts for 25% of all retail business. This is less than America but still much greater than South Africa. Although the cult of owning your own business is perhaps more strongly established in the U.S.A than in some other countries, the growth in UK franchising has also been very rapid. Europe tends to follow America in commercial practices and franchising has already established for itself a position of dominance in the retail trade. It is therefore clear, due to the insecurity of the job market and the fact that setting up one's own business may be the alternative to unemployment.

What many prospective investors and franchisees find particularly attractive is that it is ideal for those with little experience of running their own business. Franchising operates in a way that take some of the sting and isolation out of going it absolutely alone (Barrow & Golzen,

1991:12). The most compelling reason of all, however is the connotation with success. *It is reckoned that as many as 80 new businesses fail, whereas 90 % reputable franchises succeed* (Lipkin & Parker, 1999: 203). That they succeed is due to the fact that the franchisor are willing and capable to pull out all the stops to prevent them from failing. The difficulties of an outlet have to be resolved by the franchisor otherwise it reflects on his/her whole operation (Barrow & Golzen, 1991: 13).

The word “franchise” comes from the French language and means privilege or freedom (Lipkin & Parker, 1999: 203). In this sense, franchising offers people the freedom to own, manage and direct their own business. It means “being in business for yourself but not by yourself” according to Nic Louw, executive director of FASA.

Franchising is a collaboration between an independent person and a company that wishes to expand its business. This collaboration is governed by a franchise agreement. In order to expand its business the company (franchisor) allows a third party (franchisee) the right to use its trade name, business methods and know-how. In return, the franchisee, who is an independent trader, accepts certain restrictions on the way he or she conducts their business. The franchisee also agrees to make royalty payments to the franchisor. The type of franchising is often referred to as Business Format Franchising.

The term franchising is often used out of context and results in confusion between other agreements such as distributorships, agency agreements and licensing agreements.

Distributorships occur where a third party acquires goods on his account from a supplier for on-sale to customers. Such agreements will not usually require the distributor to trade under a specified name or put restrictions on the way he should run his business. The supplier's return will be obtained in the mark up he charges the

distributor. The distribution agreement will contain some restriction on the distributor relating to products to be supplied e.g. minimum quantities, servicing and guarantees.

Agency agreements are similar to distributorships except that the agent does not purchase products from the supplier but sell the products on behalf of the supplier, while charging the supplier a commission for his services.

Licensing agreements also contain some elements which are found in franchising agreements, namely the licensing of know-how, or intellectual property rights, but are usually more associated with manufacturing than marketing and seldom contain restrictions in the way that the licensee can operate his business.

1.2.2 Franchising in South Africa

Since the early 1990's South Africa has seen a franchise boom similar to the one experienced in America during the 1980's (Anon, 2000: 66). New opportunities have spring up on every street corner and for the potential franchise the choice seems endless.

Since South Africa's first democratic elections in 1994, the face of the South African business industry has changed dramatically. Retrenchments, affirmative action and the closing of companies have put thousands of people out of work. Faced with the reality of the situation, many employees who were fortunate enough to receive severance packages, invested their money into opening franchises. As a result many franchises are run by skilled people and this usually leads to a more successful system.

In South Africa, franchising accounts for only 9 % of all retail business (Lipkin & Parker, 1999: 202). However this figure is forecasted to escalate rapidly over the next 5 years. South Africa currently has over 400 franchisors. The industry had already created more than 20 000

job opportunities. An average growth of 6 % implicates that 6 000 jobs are also annually created (Lipkin & Parker, 1999: 202).

Despite this optimistic predicted growth ratio's, the industry is viewed with a lot of scepticism (Naude, 2000: 3). Credibility regarding ethical franchising is a problem. And although the Franchise Association of South Africa (representing ± 200 franchisors as affiliated members), sets standards for ethical franchising and is regarded as the unofficial "watchdog" of the industry, the industry is still rife with failure and problems.

1.2.3 The benefits/advantages and disadvantages of a franchise

While franchising eliminates some of the more costly and at times disastrous bumps in the waving curve of working for oneself, it is not an easy way to riches either.

According to Lipkin & Parker (1999: 204) there are certain advantages as well as stresses and dangers inherent to franchising.

Advantages

1. *The franchisee will start a tried and tested business concept that has been fully "pilot" tested.* Often franchisees do not have the general business management skills or specialised knowledge needed in the proposed business activity. The franchisor owns this knowledge and has the necessary business skills, which he passes on to the franchisee.
2. *The franchisor should have developed a long-term strategic business plan including a country development plan, which the franchisee will be exposed to.* The franchisor's strategic vision should provide for the growth and adaptability required for the survival of the brand. A country development plan is the geographic expansion plan that outlines the geographic areas

earmarked for expansion, as well as the rate of expansion. The rollout of the franchisee's store is therefore part of a larger expansion strategy, so the brand that the franchisee has bought into should become more valuable with time.

3. *The franchisor should use scientific site selection criteria and give the franchisee a well-calculated, protected trade area around his business.* Ideally, the country development plan should be based on a well-developed expansion strategy that incorporates the geographic requirements for the sustainability of a site, e.g. number of households or number of economically active people. This scientific site selection should ensure that each franchisee will have a viable business in his/her area.

4. *As a franchisee, you will be the owner of your own business; however, restrictions will be imposed on you by the franchise agreement.* These restrictions usually include prescriptions on the use of trademarks, marketing campaigns and standards of operating. By abiding by these prescriptions and specified standards, the risk of business failure are substantially reduced.

 5. *The franchisee will be able to make use of the franchisor's purchasing power and other benefits relating to the size of the operation e.g.*

- The franchisee should set up the business at a lower cost. The franchisor should be able to source capital equipment and shopfitting at lower prices because of bulk buying and relationships with suppliers.
- The franchisee should find it easier to raise capital. An established franchise usually has a strong brand and goodwill, which will influence a banker's decision when granting the franchisee a loan.
- The franchisee should be able to purchase goods on an ongoing basis at preferable prices. Again, this is due to

the franchisor's ability to buy in bulk and good supplier relations.

- The franchisee should be offered participation in the franchisor's medical aid and provident fund. These are benefits that an independent business may not be able to obtain at the same preferential rates.

✓ 6. *The franchisor should provide its franchisees with both initial and ongoing training both on a theoretical and practical level. The franchisor's support staff provides "on-the-job" training when visiting the site, while the franchisor should organise special courses and seminars for the franchisees and staff alike.*

✓ 7. *The franchisee should benefit from the franchisor's ongoing new product and concept development. The franchisor has the infrastructure in place to support a research and development function within the operation, or the resources to outsource this function. New product/concept development is vital for the survival of a product. However, franchisees should also be able to provide their input into product/service development.*

✓ 8. *The franchisee can take advantage of the brand name and reputation that has been developed by the franchisor. This may reduce the lead-time in making a business successful and may even reduce the amount of working capital required.*

✓ 9. *The franchisee will receive the use of proven systems and control. This includes Point Of Sale systems specifically designed for the concept and customized accounting packages,*

10. *The franchisee will tap into the franchisor's tried and tested price strategy and costing systems. The franchisor can experiment with pricing strategies in a controlled way, e.g. by testing new prices at selected company owned stores first.*

11. *The franchisee will receive an updated, workable operations manual, which will help him/her to run the business in all aspects e.g. registering the business, marketing, labour laws and production standards. The operations manual is the blueprint for running the business and must get updated regularly.*
12. *The franchisee should receive regular communication and motivation from the franchisor. The franchisor should organise an annual franchisee conference as well as other communication initiatives to keep franchisees aware of industry trends, operational decisions and marketing initiatives.*
13. *The franchisee will have a successful, proven asset to sell when deciding to move on. The value of the brand and the goodwill accumulated will contribute to this.*

Disadvantages

1. *A franchisee is subject to substantial control by the franchisor. The franchisor has to ensure that a range of operating standards must be adhered to. These restrictions are obviously absent in independent businesses. It therefore takes a special kind of entrepreneur to become a franchisee. The kind of entrepreneur who makes a successful franchisee is willing to work hard, provide his own input and, most importantly, operate within the prescribed parameters of the franchisor. Operation procedures, however may also be too rigid and inflexible.*
2. *A franchisee pays an upfront fee and ongoing royalties. This upfront fee can be substantial. The franchisee may therefore need to incur a heavy debt load to start the business. Although these fees and royalties help the franchisor in building the brand*

and supporting the franchisee, they can lead to an adversarial relationship between franchisor and franchisee.

3. *There may be restrictions on the franchisee's ability to sell the business.* The franchisor will normally have first option to purchase the business or approve the potential buyer. This may slow down the selling process and impact the selling price.
4. *The success of the franchise operation and the franchisee's business is heavily dependent on the ability of the franchisor and the other franchisees.* To a large extent, therefore, the well being of the franchisee is directly related to the sustained vision and performance not just of the franchisor but also of the other franchisees. Poor strategic decisions as well as lack of strong management and leadership skills may have serious consequences for the franchise.

1.3 SUPPOSITION

The overstatement of the unilateral authority of *franchisors*, not just in the South African franchising industry, but also in the U.S.A., are often reflected in franchise agreements that are unfair and one-sided. The idea that franchisees have the opportunity to choose among many franchise systems at the beginning of a relationship are very often conveniently forgotten and ignored. The fact is that prospective franchisees are also pioneers and entrepreneurs in their own right. As investors they are free *not* to associate with *franchisors* at all (Schultz, 1999: 2).

In franchising, the *success* of both the franchisee and franchisor is truly dependant on the success of each other (Wilkerson, 1999: 3). To succeed ultimately, however will be due to the fact that the franchisor are willing and able to use its wisdom though *success* and *failure* alike.

As mentioned, the franchising industry is involved in a lot of legal activity which does not reflect well on the industry. The question therefore is if "due diligence" is exercised properly? Secondly as final responsibility regarding success of a franchise obviously lies with the franchisor, what are the reasons for the franchisor's inability to succeed?

The surest way to assess a franchise is to judge it by its past performance (Venter, 1999: 18). If a company already has 200 successful franchisees it probably will be successful for new prospective franchisees. Being a successful business or company, and opting for franchising in order to expand, does not automatically qualify it as a future franchise success. Or render its products or services suitable as a franchise concept.

1.4 AIM OF DISSERTATION

In recent years the South African market has seen quite a number of failed franchises, which have cost investors and franchisees substantial sums of money. What is clearly needed is regulation of the industry through legislation. As well as applying and exercising careful franchise "due diligence".

The aim of this dissertation will be to:

- To compile a profile of a successful *franchisor* in the S.A. franchise industry in order to exercise such franchise "due-diligence".
- In specific to evaluate the franchisor as entrepreneurial leader and to determine the specific strategic management and leadership skills necessary for long-term success and growth. Hopefully this will provide valuable guidelines and insight for prospective

franchisees to benchmark investment opportunities in the franchise industry.

1.5 METHOD OF STUDY

In order to determine this profile, a theoretical study of the franchisor as entrepreneurial leader, and the defining and rating of certain strategic management and leadership skills needed to be a successful franchisor has been done. A field study by means of structured interviews, questionnaires as well as follow-up telephonic discussions were conducted in compliance with 10 successful franchisors in the South African franchise industry, in order to determine the importance of these skills.

1.6 PROGRESS OF STUDY

In chapter 2 the many forms of franchising will be discussed. The business format franchising option, as dominant type in South Africa, as well as its main features will be explained. Notwithstanding the existence of a code of ethics applicable to the South African franchise industry, numerous problems and challenges are the order of the day. The FASA code of ethics as well as the foundations necessary for a successful franchisor-franchisee relationship will also be discussed.

Chapter 3 will be a theoretical study and discussion of the franchisor as entrepreneurial leader, and the specific entrepreneurial skills needed in order to be a successful franchisor. The most important strategic management and leadership skills needed will also be discussed and explained.

Chapter 4's intent will be to determine the importance of the most important strategic management and leadership skills of the franchisor as entrepreneurial leader. This will be done by means of a field study through structured interviews, questionnaires and telephonic

discussions which will be conducted with 10 well-known franchisors in the South African franchise industry.

The dissertation will conclude in chapter 5 with the deduction that would-be investors and franchisees should exercise franchise “due-diligence” by attaching utmost importance to the strategic management and leadership skills of the franchisor. A short summary of the most important skills and practises of the successful entrepreneurial franchisor will also be supplied.

CHAPTER 2

THE SOUTH AFRICAN FRANCHISE INDUSTRY

2.1 BACKGROUND

Franchising as described in chapter 1, is an established concept not only in South Africa, but also in the U.S.A, Australia, the UK and Europe. It is also very much an old established concept. Evidence suggests uses of this concept in China as far back as 200 B.C. Mendelsohn, a well-known franchise expert, through his research, also found evidence of franchising during the eleventh century. Queen Isabella granted to Christopher Columbus a “franchise” to establish trade links with the new world during his voyages (Fick, 1998: 11).

There are many forms of franchising (Barrow & Golzen, 1991: 15). The term franchise covers a wide variety of arrangements under which the owner of a product, a process, a service or even just a name having certain connections (e.g. that of a sportsman) licenses another to make or use something in exchange for some form of payment. This can be either direct, in the form of a fee and/or a royalty, or indirect in the shape of an obligation to buy a service or a product in which the license holder has some kind of commercial interest. An example of the latter is the English tied pub, where the license has to obtain his supplies from a particular brewery. This type of arrangement has been around since the 16th century. Very often the brewery owned the premises, equipment as well as stock. The owner or manager also had to stake in the business, often just supervising. This type of arrangement however, proof to be very “one-sided” and differs to the modern concept of franchising.

The word franchise means privilege or freedom and in this sense it offers people the freedom to own, manage and to direct their own business. It means being in business for yourself but not by yourself.

Franchising is an arrangement between the franchisor (the seller or grantor of a privilege) and the franchisee (the recipient or purchaser of a privilege). The franchisor owns the right to the name or trademark of the business whilst the franchisee purchases the right to use the trademark and system of business. There are a number of different franchising options but the most familiar types are:

1. **A distributorship**

A distributorship for a particular product, such as a make of car. This is also sometimes referred to as an *agency*, but there is a fundamental difference between these two concepts. An agent acts on behalf of a principal. Even though he is not employed by him, and even though he may have an agency for the products and services of more than one principal, what the agent does, says or represents to third parties is binding on the principal in question, as if they were employer and employee. A distributorship, however, is an arrangement where both parties are legally independent, as vendor and purchaser, except that the purchaser, in exchange for certain exclusive territorial rights, backed up by the vendor's advertising, promotion and, possibly, training of his staff, will be expected to hold adequate stock and maintain his premises in a way that reflects well on the vendor's product or service.

2. **A license to manufacture**

A license to manufacture a certain product within a certain territory and over a given period of time, have access to any secret process this involves and use its brand name in exchange for a royalty on sales.

This arrangement resembles a dictatorship. Licensor and licensee are independent of each other, except that the licensor will no doubt insist that the licensee complies with certain

specifications as regards content and quality in order to preserve the good name of his product.

3. The use of celebrity name

The use of a celebrity name to enhance the sales appeal of a product and guarantee, at least by implication, its quality.

The most common example is the endorsement, by a sports personality, of equipment associated with his activity and bearing his name, in return for a royalty payment by the manufacturer.

4. The use of a trade mark

Here a widely recognised product is exploited commercially for a fee and subject to certain licensing conditions, rather than the name of an individual.

5. Business format franchising

Although all the above forms of franchising continue to flourish, it could be said that business format franchising has emerged as the dominant and certainly the most rapidly expanding type, as is also the case in South Africa. This is because it meets the commercial needs of the present time. Looking back into the history of franchising, it is interesting to note that distributorship franchises were first applied to Singer sewing machines after the American Civil War, when the USA emerged as a vast market, but when communications were too poor across great distances to make centralised distribution effective (Barrow & Golzen, 1991: 18).

The concept was picked up by the motor car industry, though the problem there was somewhat different; not so much, at that time, of finding a mass market, but more one of establishing outlets to provide display space, back-up service and, of course,

to buy the actual cars. Plainly the manufacturers could not afford to set up distribution outlets and finance stock as well as make the cars (Barrow & Golzen, 1991: 18).

The success of such forms of franchise encouraged numerous imitators from the twenties to the fifties, during which time the trend was to rationalise small, locally based manufacture into national and even multi-national entities. This did, however, cause problems of sales and distribution. Local industries, aware of local market conditions, were shown in many cases to have been rather more successful in this respect than “faceless corporations” located a long way distant. The answer was to re-create, in some way, the virtues of local industry by franchised distribution and licenses. From the point of view of the franchisor, these arrangements turned out to have other advantages as well over the costly alternative of keeping total control by setting up national networks of salesmen and warehouses to cover a region – and in the post-war period, overseas countries. The franchisee was usually more dedicated to the interests of the franchisor, in whose success he stood to share, than many a salaried employee would have been. This was true even when the franchisee was also trading in goods and services other than those for which he held a franchise – indeed distributorship franchises were often arrangements which placed no great obligation on the franchisor and gave equal freedom to the franchisee.

Business format franchising incorporates elements from all these earlier ideas and combines them in a way that is particularly suited to current circumstances and economic conditions (Barrow & Golzen, 1991: 18). It is characterised by an ongoing relationship between the franchisor and franchisee that includes not only the product, service and trademark, but enables the franchisee to acquire the right to use the

franchisor's name, goodwill, products and services, operating manuals and standards, quality control, marketing procedures, administrative and operational systems and support facilities.

Shortly its main features are:

1. It is a license for a specific period of time to trade in a defined geographic area under the franchisor's name and to use any associated trade mark or logo.
2. An activity is franchised or a service, which has already been tried and tested to produce a formula of operating that has been found to work elsewhere.
3. The franchisor provides the entire business concept of that formula (usually called the "blueprint") for the conduct of operations. This must be followed by the franchisee. In fast food, for instance, the ingredients of any "secret" recipes for the type of food being offered are strictly laid down, as are the specifications for the surroundings in which it is served.

The blueprint is generally set out in an operating manual which is given to the franchisee when negotiations are completed.

4. The franchisor educates the franchisee in how to conduct the business according to the method laid down in the blueprint.
5. The franchisor also provides back-up services in order to ensure that the franchise operates successfully. This should certainly cover advertising and promotion of the franchise's name in general and may also cover promotion of the particular franchise in its locality. It can cover many other aspects: ongoing business advice including help in raising finance, market research into the liability of a particular occasion for trading purposes, assistance with negotiating leases and obtaining planning

permissions, site development, the provision of building plans and specifications, a standard accounting system – virtually anything connected with setting up a new business.

6. In exchange for the business blueprint and the services the franchisor provides, the franchisee is expected to make an initial investment in the business and to pay a weekly or monthly royalty to the franchisor thereafter, normally based on turnover. There may also be an obligation on the franchisee to buy some or all goods and equipment from sources nominated by the franchisor. When the franchisor benefits financially from such an arrangement, acting in effect in the role of a wholesaler, the royalty will be lower. In some cases, in fact, there may be none at all.
7. The participation of the franchisor in setting up the business does not mean that he owns it. It belongs to the franchisee and he is free to dispose of it, though he will probably have to give the franchisor first refusal and obtain his approval of the person the business is sold to, if the franchisor does not want to take it off his hands (Barrow & Golzen, 1991: 20).

2.2 FORMAL DEFINITION OF A FRANCHISE

A contractual license granted by one person (the franchisor) to another (the franchisee) which:

- a) permits or requires the franchisee to carry on during the period of the franchise a particular business under or using a specified name belonging to or associated with the franchisor; and
- b) entitles the franchisor to exercise continuing control during the period of the franchise over the manner in which the franchisee carries on the business which is the subject of the franchise; and

- c) obliges the franchisor to provide the franchisee with assistance in carrying on the business which is the subject of the franchise (in relation to the organisation of the franchisee's business, the training of staff, merchandising, management or otherwise); and
- d) requires the franchisee periodically during the period of the franchise to pay to the franchisors sums of money in consideration for the franchise of for goods or services provided by the franchisor to the franchisee; and
- e) which is not a transaction between a holding company and its subsidiary or between subsidiaries of the same holding company or between an individual and a company controlled by him.

The last clause establishes the important distinction between a franchise and an agency; though this official definition is certainly useful, it does not mention a number of aspects which are important from the point of view of the person taking up a franchise (Barrow & Golzen, 1991: 22). It does not indicate that an initial fee is usually payable by the franchisee nor does it stress that the subject of the franchise should be a tried and tested commercial operation (though running a pilot scheme is a condition of membership of FASA). It does not mention, further, that the business, once set up, is the property of the franchisee, nor does it warn him of the degree of control he may be subject to under clause b). Further, it gives no indication of the extent of the back-up services that the franchisee might reasonably expect to get for his money. In other words, the definition is not an adequate measure against which to check the franchise contract, which requires the exercising of careful "due diligence". Seen in the light of non-existent legislation, it also requires the need for perspective and insight regarding a particular franchise concept. As well as information and knowledge regarding the specific capabilities of the franchisor behind it.

2.3 THE ETHICS OF FRANCHISING

The Franchise Association of Southern Africa (FASA) was incorporated in 1979 as a non-profitable organisation due to the increasing interest and growth of the concept (Stone, 2000: 46).

The value and need of such a body was first identified by the Johannesburg Chamber of Commerce. FASA was therefor established under the auspices of the Chamber. Income are generated from membership fees, events eg. seminars and an annual franchise exhibition as well as the selling of publications. Profits are geared towards the promotion of the franchise concept.

FASA was born out of the belief that although the franchise concept do hold certain definite advantages for the prospective investor and franchisee, the very concept also risks being misused not only to the detriment of franchisees but also the franchise concept and industry as such. Therefore FASA has established a general Code of Conduct which sole purpose is the upholding of Ethics in Franchising. This Code applies to all members and is the nucleus of the Business Practices Committee's Consumer Code for ethical standards in the franchise industry (FASA, 1996).

THE FASA CODE OF ETHICS AND BUSINESS PRACTICES

1. Members of FASA take cognizance of the Business Names Act 1970, the Harmful Business Practices Act and similar legislation.
2. No member shall offer, sell or promote the sale of any franchise, product or service by means of any explicit or implied representation which is likely to have a tendency to deceive or mislead prospective purchasers of such franchise, product or service.

3. No member shall imitate the trademark, trade name, corporate name, slogan, or other market identification of another business in any manner or form that would have the tendency or capacity to mislead or deceive.
4. The pyramid or chain distribution system is inimical to prospective investors and to the franchise system of distribution and no member shall engage in any form of pyramid or chain distribution.
5. An advertisement considered in its totality shall be free from ambiguity and, in whatever form presented, must be considered in its entirety and as it would be read and understood by those to whom directed.
6. All advertisements shall comply in letter and spirit with all applicable rules, regulations, directives, guides and laws promulgated by any governmental body or agency having jurisdiction.
7. An advertisement containing or making reference, directly or indirectly, to performance records, figures or data in respect of income or earnings of franchisees shall be factual, and, if necessary to avoid deception, accurately qualified as to geographical area and time periods covered.
8. An advertisement containing information or making reference to the investment requirements of a franchise shall be as detailed as necessary to avoid being misleading in any way and shall be specific with respect to whether the stated amount(s) is/are partial or the full cost of the franchise, the items paid for by the stated amount(s), financing requirements and other related costs.

9. At least seven calendar days prior to the signing of any franchise agreement, the franchisor shall provide the prospective franchisee with a written disclosure document which shall contain the information set forth in Appendix 1 to the Code of Ethics and such other information as may be material to the franchise offered.

All franchise agreements will contain a clause referring to the disclosure documents and recording that the information therein contained is, to the best of the franchisor's knowledge and belief, true and accurate and that no material information has been withheld.

10. All matters material to the franchise relationship shall be contained in one or more written agreements, which shall clearly set forth the terms of the relationship and the respective rights and obligations of the parties.
11. A franchisor shall select and accept those franchisees who, upon reasonable investigation, appear to possess the basic skills, education, personal qualities and financial resources adequate to perform and fulfil the needs and requirements of the franchise. In this regard, a franchisor shall not discriminate in this selection process on the basis of race, colour, religion, age, disability or sex. A franchisor may grant franchises to some franchisees on more favorable terms than are granted to other franchisees as part of a programme to make franchises more widely available.
12. In his own internal management structure, the franchisor will not discriminate on the basis of race, colour, religion, age, disability or sex. In addition, the franchisor should endeavor to introduce such previously disadvantaged people into his management structure for training and possible advancement in the company.

13. The franchisor shall encourage and/or provide training designed to help franchisees improve their abilities to conduct their franchise.
14. A franchisor shall provide reasonable guidance and supervision over the business activities of franchisees for the purpose of safeguarding the public interest and of maintaining the integrity of the entire franchise system of the benefit of all parties having an interest in it.
15. Fairness shall characterise all dealings between a franchisor and its franchisees. To the extent reasonably appropriate under the circumstances, a franchisor shall give notice to its franchisee of any contractual breach and grant reasonable time to remedy defaults.
16. A franchisor should be conveniently accessible and responsive to communications from franchisees, and provide a mechanism by which ideas may be exchanged and areas of concern discussed for the purpose of improving mutual understanding and reaffirming mutuality of interest.
17. A franchisor shall make every effort to resolve complaints, grievances and disputes with its franchisees with good faith and good will through fair and reasonable direct communication and negotiation. Failing this, consideration should be given to mediation or arbitration.
18. On request from the franchisee, the franchisor shall make full disclosure of any form of incentive he might derive from the franchisee being bound to deal with certain nominated companies/firms.

To be regarded as ETHICAL FRANCHISING, the franchising concept is also characterised by a second requirement for the benefit of both the franchisor and the franchisee. A Disclosure Document is necessary to ensure a healthy relationship between franchisor and franchisee (see Annexure A). The requirements for this document are therefore aimed at a full and complete disclosure of a particular franchise business.

A written disclosure document must be provided to a prospective franchisee who must then have at least seven calendar days (calling off period) to review the contents and information before signing an agreement or paying any fees.

The disclosure document contains all relevant information about a franchisor as may be material to the franchise offered. This includes for instance, an auditor's certificate certifying that the business of the franchisor is a going concern, key financial information, summary of the main particulars and features of the franchise and a list of components making up the franchise purchase.

2.4 THE FRANCHISOR AND FRANCHISEE RELATIONSHIP

Franchising should be based on mutual trust, respect and understanding between the franchisor and the franchisee (FASA, 1996: 3). To be successful this relationship requires:

- total acceptance by both of a common vision, mission and values
- good communication at all levels
- support in both good and bad times
- a desire and dedication to succeed
- maintaining and upholding clearly defined operating procedures and quality standards
- contribution to growth through feedback, research and development, and promotion

Franchising has proved to be extremely popular and successful. It has also proven its credentials in 70 industries in more than 100 countries throughout the world. According to FASA (1996: 3) inherent to the success of franchising is that it is based on:

- a proven concept
- a mentorship that lasts the life of the franchise agreement
- lower risk and less chance of failure
- not being a “master/servant” but a business relationship

According to Stone (2000: 46), the benefits of joining the Franchise Association of South Africa are numerous. Credibility is the first of these. The *franchisor* who is a member of FASA becomes a part of an *ethical team*, building a good reputation for the franchise industry in South Africa. “Ethical franchising is honest franchising” says Nic Louw (2000: 46), executive director of FASA. *Trust, integrity and reliability* should be the most important priorities concerning the franchisor-franchisee relationship. Without these, there can never be a partnership between the parties.

Problematic however, are that “trust and integrity” as specific leadership criteria, cannot be measured easily. Also contradictory is the fact that although the final responsibility for long-term success and growth of a franchise lies with the franchisor, franchisees and would-be investors are continuously warned to exercise due-diligence. Responsible ethical franchising should be about the franchisor doing “his homework” before embarking or making use of franchising to expand his business. This “homework” entails thorough strategic planning of operations, marketing planning as well as proper service or product planning.

Probably the most important aspect of this planning should be the exact positioning of the franchisor as entrepreneurial leader. As a business leader, the franchisor should value “total customer satisfaction” and understand that it represents the ultimate service ethic. As a leader he/she must strive for total stakeholder satisfaction, caring for *all* who have a stake in the success of the

operation (Covey, 2000: 27). To bring about this, synergy is needed. Only synergy is, and will be able to combine ethics, integrity and trust. The second activity needed is alignment. This will assure that the proper organisational structure, systems and operational processes can be put in place and are able to effectively contribute towards achieving this vision and mission of meeting customer and other stakeholders needs (Covey, 2000: 26).

2.5 **PROBLEMS AND CHALLENGES FACING THE SOUTH AFRICAN
FRANCHISE INDUSTRY**

Of great concern is the fact that the franchise industry in South Africa as mentioned in Chapter 1, is currently viewed with a lot of scepticism and lack of credibility (Naude, 2000: 3). Problems in the industry also prompted SUCCEED to do a series of investigative articles during the end of 1999 (see exhibits 2.1. and 2.2).

Exhibit 2.1 **Problems and challenges facing the South African
franchise industry**

IN THE PUBLIC INTEREST

**The saddest
franchise stories**

We feel that we have a moral obligation to run the following article. We have accepted advertising from most of the businesses mentioned in it and our back copies are still being read by many people.

Source: Venter, 1999: 18.

The ethics of franchising

- what to look for, what to avoid – we ask the experts

Those saddest stories

An article entitled "The saddest franchise stories" in the August/September issue of SUCCEED Magazine has caused a stir in franchise circles. In it we decried certain elements in the industry that were either not ready to franchise or purposefully trying to defraud prospective franchisees. Altogether 15 franchises that should be avoided were named in the article. We expected a flood of lawyer's letters on publication, but only received one, demanding that we apologise to their client. We did receive many letters though. They came primarily from franchisees who had lost money. We also received numerous complaints from shopfitters, designers, a chef, an advertising agency, a printer, a plumber and others who had not been paid by some of these people. We still have a few copies of the August/September issue. Anyone who would like a copy, should phone our subscription manager, Kallern Rajdoe, on (011) 646 4767.

Source: Venter, 1999: 23.

"Look before you leap!", "what to look for, what to avoid?" are headings regularly found in business magazines promoting the franchise industry in South Africa. It would very much seem that the industry is facing some of its toughest challenges since its inception. Bendeta Gordon (former Parker-Gordon associate) already in 1995 (Anon: 6) explained that franchising is too often perceived to be an easy way to expand an existing business without relinquishing control over the enterprise. She urged franchisors to recognise that franchising intrinsically involves empowerment of the small entrepreneur. And that the success of any franchising arrangement is wholly dependant on the *relationship* between franchisor and franchisee.

Eric Parker, director of the franchise department of Deloitte & Touche also realises the problems the industry are facing. In a survey done by Naude (2000: 11), he conveyed the following pressing concerns:

1. The lack of an overall entrepreneurial spirit in South Africa.
2. The lack in the industry, in realising the potential of a new breed of would-be entrepreneurs eg. the previously disadvantaged and relative young professionals losing their jobs.
3. The lack of proper legislation to effectively counter act unethical franchise practices.
4. The lack of financial initiatives towards supporting prospective investors and franchisees.

Parker admits that FASA's biggest problem is, that although it is the "unofficial" watchdog of the industry, it hasn't got "any teeth" to regulate and protect the industry, specifically franchisors and franchisees, members as well as non-members of the organisation, regarding unethical conduct. He cautioned would-be franchisees already in 1995 (Anon: 6) that the industry has no regulatory body and limited support mechanisms. To date, the only main mechanisms are:

- The Small Business Development Corporation (SBDC) offers a list of service-providers to the franchising sector;
- The franchising Association of SA (FASA) provides general support and a code of ethics, but its jurisdiction is bound by its membership;
- There is as yet no official franchisee organisation;
- The Competition Board keeps a watchful eye on the industry and can be approached as a possible channel of recourse for disgruntled franchisees;
- The government has no franchising advice facility despite its stated goal of small business development.

Franchising failures in South Africa usually represents three types. The first type of failure is usually the franchise that came into the industry purely to sell franchises (Venter, 1999: 18). There is, often to the detriment of the franchisee who has signed a four or five year legally binding contract, no substance to the business at all. They never had any intention of ever providing the franchisee with anything. From the start, the only aim was to collect money.

Some as affiliated and accredited members of FASA, also fail, notwithstanding the fact that they had detailed disclosure documents, contracts and operation manuals, compiled by leading franchise developers. These franchises are not necessarily run by dishonest people. They are simply business failures. They may have started from an existing successful business. But like so many entrepreneurs, the leaders of the business made mistakes. Quite often, it wasn't a business suited to franchising, or a viable franchise concept.

The third type are those that also start out well, but as they get into trouble they take the route of trying to stay afloat by selling franchises and living off franchise fees. A franchise structure and brand name is never built and inevitably the company dies.

Franchising is probably the single invention that has brought more wealth to ordinary people than any other. It is also unfortunately an area that is perfectly suited to rip-off artists and failing brands wanting to sell franchises to prop up a failing business (Venter, 1999: 18).

This is indeed not very good news for the would-be investor or franchisee, responding to the "puffing" going on in the industry as mentioned in chapter 1. Franchise supporting-and-training ventures are also mushrooming. New team on the block is Franchise Partners, a joint venture between leading franchise consultancy; Franchise Directions, and finance house, Business Partners. This new finance,

training and mentorship company concentrates not on financing individual outlets, but on using equity finance to develop the franchise itself (Anon, 2000: 24). Quite a few tertiary education institutions are also running short franchising educational programmes.

However, all this endeavors does not decrease the risk a would-be franchisee or investor faces when wanting or “leaping” into franchising. Unfortunately, in reality FASA is a body representing only franchisors as affiliated members. Franchise developers eg. Franchise Partners support franchisors, and franchising in general in South Africa do still represent the old industrial-age model of the labour employer-employee relationship (Schultz, 1999: 1). It is still “them” against “us”. “Them” represented by franchisees and franchisors *not* affiliated to FASA. “Us” represented by FASA members and franchise developers profiting from and creating job employment in the industry.

Research done by Naudé (2000: 3) found that there are currently more than 400 franchises and concepts in South Africa. Interesting is that just 45 % (200 franchise systems) are affiliated to FASA. Some of the most successful franchise groups are not members. Which poses the question if membership to FASA should really be seen as such an important criterium when considering to invest in a franchise.

As explained, the lack of legislation as well as disciplinary powers in the industry renders FASA useless when the very important relationship between *franchisor and franchisee* start to deteriorate and disintegrate. Even with its mediatory and arbitrationary powers, which are a prerequisite clause in any standard franchise contract, FASA is known to withdraw when relationships disintegrate and become legal.

Another important prerequisite necessary for FASA membership is a “win-win” contract between franchisor and franchisee, as well as a

professional operational manual. According to Mr Nic Louw, CEO of FASA, it has been found, upon investigation that very little contracts are “win-win” and therefor some franchisors membership had been provoked, as contracts were altered and manuals were found to be nothing more than “window-dressing”. Which leaves the would-be investor and franchisee very much out in the cold.

It is therefore very clear that there is more to franchising in South Africa than meets the eye. At this stage potential entrepreneurs are left wide open to the industry’s unfolding pitfalls. Due to the nature of the concept, it is unfortunately true that a franchise usually “fails” from the top and not the bottom as mentioned in chapter 1. Reasons usually are *a lack of planning, lack of strategic management and leadership skills and most of the time unethical business practices*. Such is the nature of this one-sided relationship that would be franchisees are nowadays required to complete a “ee-test” (Lipkin & Parker, 2000: 210). This is usually the first step in the process of identifying a potentially successful franchise holder. The test assesses sales and marketing competency, ability to comply with franchise requirements, leadership, customer orientation and resilience.

“But what about the *franchisor*”? This is obviously the question. As the responsibility for success clearly lies with the franchisor, *how* should and could a would-be franchisee determine the most important skills and capabilities necessary for long-term success of a franchise?

In this chapter, in-dept information concerning the franchise industry as well as the challenges and problems facing the industry were discussed and identified.

Finally the controversial franchisor-franchisee relationship and need for careful franchise “due-diligence” was discussed.

In the next chapter, relevant skills and specifically the strategic management and leadership skills of the *franchisor* in the South African franchise industry will be determined, in order to assist investors and would-be franchisees towards exercising careful franchise "due diligence".

CHAPTER 3

SKILLS NECESSARY TO BE A SUCCESSFUL SOUTH AFRICAN FRANCHISOR

3.1 THE FRANCHISOR AS ENTREPRENEURIAL LEADER

“Who can be an entrepreneur you ask?

Anyone who wants to experience the deep, dark canyons of uncertainty and ambiguity; and who wants to walk the breathtaking highlands of success. But I caution, do not plan to walk the latter, until you have experienced the former.” An Entrepreneur (Timmons, 1999: 27)

Entrepreneurship is a way of thinking, reasoning and acting that is opportunity obsessed, holistic in approach, and leadership balanced (Timmons, 1999: 27). Entrepreneurship results in the creation, enhancement, realisation and renewal of value, not just for owners, but for all participants and stakeholders. At the heart of this process is the creation and/or recognition of opportunities, followed by the will and initiative of seize these opportunities. It requires a willingness to take risks – both personal and financial.

Van Aardt, Van Aardt & Bezuidenhout (2000: 5) shares Timmon’s view and define entrepreneurship as “the act of initiating, creating, building and expanding an enterprise or organisation, building an entrepreneurial team and gathering other resources to exploit an opportunity in the marketplace for long-term gain”.

Today entrepreneurship has evolved beyond the classic startup notion to include companies and organisations of all types, in all stages. Such is the case also within the franchise industry. Most franchisors as well as franchisees are typical entrepreneurs. They only differ in

the respect that business activities and operations are channeled through a specific franchise concept.

Entrepreneurial leaders inject imagination, motivation, commitment, passion, tenacity, integrity, team work and vision. They have dilemmas and must make decisions despite ambiguity and contradictions. Very rarely is entrepreneurship a get-rich quick proposition rather, it is one of building-and continually renewing-long-term value.

According to Timmons (1999: 31), one of the biggest mistakes entrepreneurs, therefor also franchisors make is *strategic*: they think too small. The chances for survival and success are lower in small job-substitute ventures. Even if they do survive, they are less financially rewarding. Therefore, the risk and fear are not really worth the effort.

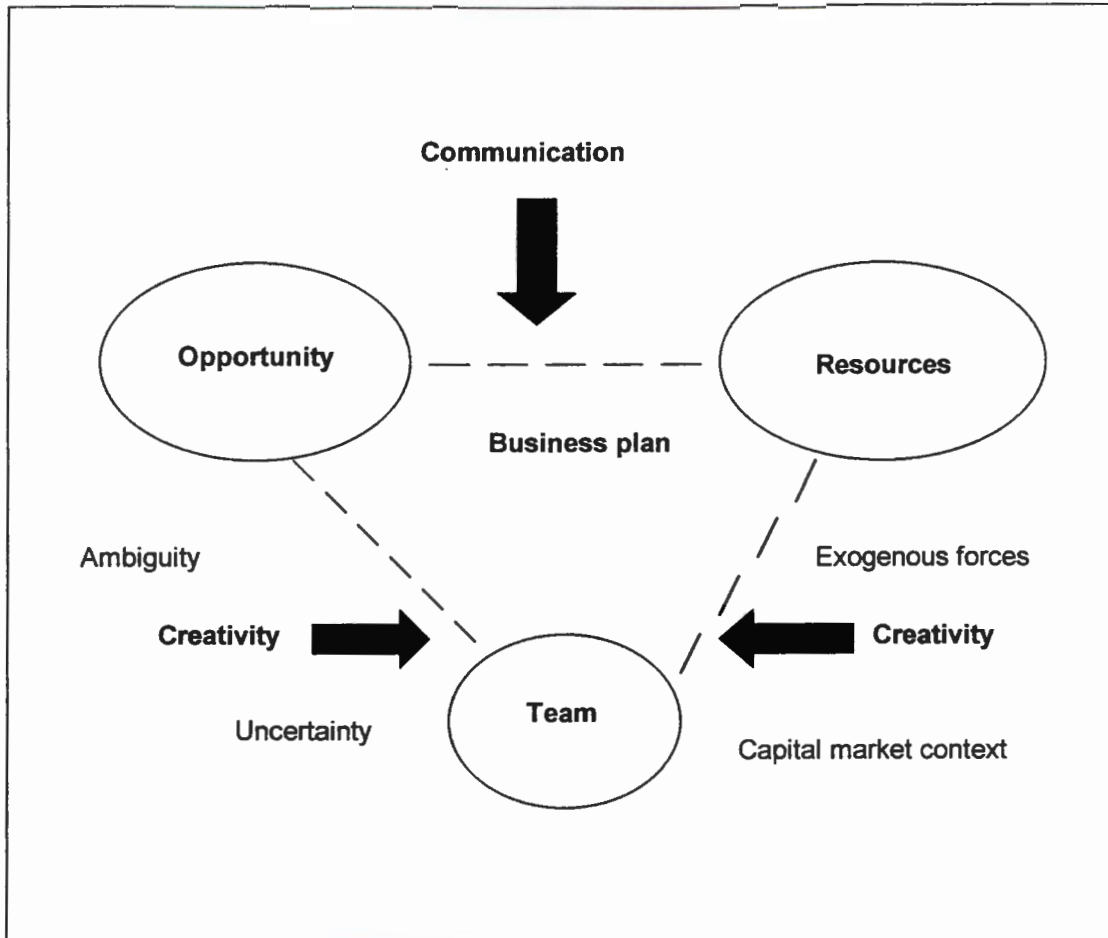
Unfortunately, the record of survival is not good among all firms started. This is also the reason why franchising is usually sought as an easier, safer avenue towards business success. This offer ends in disaster and failure. Most smaller enterprises that exercise this option simply do not meet the notion of entrepreneurship. They do not create, enhance or pursue *opportunities* that realise *value*. They tend to be job substitutes in many instances, and they are usually *undercapitalised, unmanaged and poorly located* (Timmons, 1999: 33).

What do talented and successful high-potential entrepreneurs then do differently? According to Timmons (1999: 37) it boils down to *value creation*. And its driving forces are:

- It is *Opportunity* driven.
- It is driven by a strong *Lead Entrepreneur* and very often also a strong *Entrepreneurial Team*.

- It is *Resource Parsimonious* and *Creative*.
- It is *Integrated* and *Holistic*.

Exhibit 3.1 Model of the entrepreneurial process



Source: Timmons, 1999: 38.

There is little dispute today that the lead entrepreneur and the entrepreneurial team is the key ingredient in the higher potential venture. Investors are captivated by creative lead entrepreneurs. The ability and skill in attracting other key management members is also one of the most valued capacities investors look for. The founder who becomes the leader does so by building heroes in the team: by a philosophy that reward success and supports honest failure, that

shares wealth with those who help create it; by setting high standards for both performance and conduct (Timmons, 1999: 40).

Exhibit 3.2 The Entrepreneurial leader and team is the key ingredient for success.

An entrepreneurial leader

- Learns and teaches – faster, better
- Deals with adversity, is resilient
- Exhibits integrity, dependability, honesty
- Builds entrepreneurial culture and organisation

Quality of the team

- Relevant experience and track record
- Motivation to excel
- Commitment, determination, and persistence
- Tolerance of risk, ambiguity, and uncertainty
- Creativity
- Team focus of control
- Adaptability
- Opportunity obsession
- Leadership
- Communication

Source: Timmons, 1999: 40

Dearlove (1999: 11), identified the very same key ingredients with his research on Bill Gates of Microsoft, the greatest and well-known entrepreneurial leader today. According to him, Gates and Microsoft are largely inseparable and Microsoft attributes its success to five important factors:

- a long term approach;
- results orientation;
- teamwork and individual drive;
- a passion for its products and customers and
- continuous customer feedback.

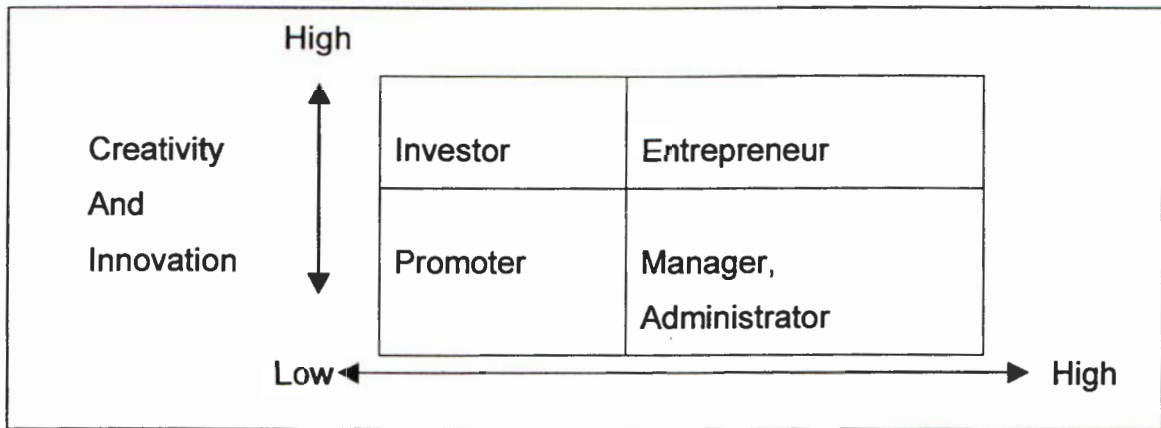
3.2 LEADING PRACTICES OF SUCCESSFUL LEADING ENTREPRENEURS

Successful entrepreneurs seem to be of both sexes and in every imaginable size, shape, color and description (Timmons, 1999: 44). However, the real question is, *What do successful entrepreneurs do?* This question is certainly just as relevant if not even more concerning the franchisor as entrepreneur. How do they think, what actions do they initiate and how do they go about building business?

Research by Timmons (1999: 44) stresses that successful entrepreneurs work hard and are driven by an intense commitment and determined perseverance; they strive for integrity; they burn with a competitive desire to excel and win; they actively seek opportunities to improve almost any situation; they use failure as a tool for learning and favour effectiveness above efficiency.

Entrepreneurs who succeed possess not only a creative and innovative flair, and other attitudes and behaviors, but also solid *management skills and business know-how* (Timmons, 1999: 45). Investors thought, often lack these necessary management skills and business know-how (Timmons, 1999: 45). Administrators govern, police and ensure the smooth operation of a business; their management skills, while high, favour efficiency and creativity is usually not required. Ideally, to be successful, the franchisor as entrepreneur should possess all of these skills with the emphasis on *recognising opportunity*.

Exhibit 3.3 Who is the successful entrepreneur?



Source: Timmons, 1999: 46

Careful analysis by Dearlove (1999: 12-15) reveals the following secrets that explain Bill Gates and Microsoft's remarkable success:

- Being in the right place at the right time;
- technical brilliance;
- obsessive desire to win and survive;
- radically different leadership style;
- focussed vision;
- unique flat and lean management and operational style;
- the ability to learn from past mistakes and not repeating it and
- the ability to attract outstanding relevant skills and capabilities.

According to Van Aardt, Van Aardt & Bezuidenhout (2000: 9), to date no single researcher has been able to pinpoint exact traits that will predict whether or not one will be successful as an entrepreneur. The following characteristics identified by them, however, compliment the views and research of Timmons and Dearlove:

- a desire to achieve;
- hard workers;
- nurturing quality;
- accepting responsibility;

- reward oriented;
- optimistic;
- excellence-oriented;
- good organisers and
- money-orientated.

Finally, evidence increasingly suggests that *experience* and *managerial know-how* is central to successful venture creation (see exhibit 3.3). Evidence also suggests that success is definitely linked to thoughtful *planning* and *preparation* (Timmons, 1999: 46). According to Timmons (1999: 46), leading practices of successful entrepreneurs are:

Marketing practices

- Deliver products and services that are perceived as highest quality to expanding segments.
- Cultivate pace-setting new products and services that stand out in the market as best of the breed.
- Deliver product and service benefits that demand average market or higher pricing.
- Generate revenue flows from existing products and services that typically sustain approximately 90 % of the present revenue base while achieving flows from new products and services that typically expand revenue approximately 20 % annually.
- Generate revenue flows from existing customers that typically sustain approximately 80 % of the ongoing revenue base while achieving flows from new customers that typically expand revenue flows by about 30 % annually.
- Create high-impact new product and service improvements with development expenditures that typically account for no more than approximately 6 % of revenues.
- Utilise a high-yielding sales force that typically accounts for approximately 60 % of marketing expenditures.
- Rapidly develop broad product and service platforms with

complementary channels to expand a firm's geographic marketing dimensions.

Financial practices

- Anticipate multiple rounds of financing (on average every 2.5 years).
- Secure funding sources capable of significantly expanding their participation amounts.
- Utilise financing vehicles that retain the entrepreneur's voting control.
- Maintain control of the firm by selectively granting employee stock ownership.
- Link the entrepreneur's long-term objectives to a defined exit strategy in the Business plan.

Management and leadership practices

- Use a collaborative decision-making style with the top management team.
- Accelerate organisational development by assembling a balanced top management team with or without prior experience of working together.
- Develop a top management team of three to six individuals with the capacity to become the entrepreneur's entrepreneurs.
- Align the number of management levels with the number of individuals in top management.
- Establish entrepreneurial competency first in the functional areas of finance, marketing and operations.
- Assemble a balanced board of directors comprised of both internal and external directors.
- Calibrate strategies constantly with regular board of directors meetings.
- Involve the board of directors heavily at strategic inflection points.

- Prepare detailed written monthly plans for each of the next 12 to 24 months and annual plans for three or more years.
- Establish functional planning and control systems that tie planned to actual performance and adjust management compensation accordingly.
- Share with employees periodic planned versus actual performance data that is directly linked to the business plan.
- Link job performance standards that have been jointly set by management and employees to the business plan.
- Prospectively model the firm based on benchmarks that exceed industry norms, competitors and the industry leader.

3.3 COMMON ELEMENTS IN SUCCESSFUL INTRAPRENEURSHIP

Studies have indicated that 90 % or more of founders started their ventures in the same marketplace, technology or industry that they have been working in (Timmons, 1999: 46). Increasingly to be found however, is corporate companies wanting to keep the internal organisation responsive and innovative. Such companies are usually lead by effective entrepreneurial leaders promoting organisational cultures which promotes thinking, cooperation, innovation and proaction (Kreitner & Kinicki, 1998: 633).

A flexible responsive and innovative internal environment is critical in certain fast-moving industries, in competitive markets as well as companies with widely diversified business portfolios (Thompson & Strickland, 1998: 352). Special pains should be taken therefor to foster, nourish and support the *intrapreneur* who are willing to champion new technologies, new services, new products and are eager to try carrying out their ideas (see exhibit 3.4). Above-all would-be intrapreneurs who advocate radical or different ideas must not be looked on as disruptive or troublesome. In the franchise industry, it is usually these intrapreneurs who create added wealth for their

companies by effectively leading the franchise divisions of their respective companies.

Exhibit 3.4

COMMON ELEMENTS IN SUCCESSFUL INTRAPRENEURSHIP

1. Feelings are the Intrapreneurs' primary motive. They feel passionate and are committed to an idea. Emotional focus is the key.
 2. Intrapreneurs usually serve all stakeholders of the organisation. They are however, willing to leave an organisation to pursue an idea.
 3. Intrapreneurs need support and assistance from across the organisation.
 4. Intrapreneurs are leaders who empower others.
 5. Intrapreneurs have a long-term perspective, yet a sense of urgency.
 6. Intrapreneurs are problem solvers. They expect problems to occur and they solve them.
 7. Intrapreneurs have the ability to attract resources, support and information within the organisation.
 8. Successful intrapreneurs are effective communicators. They are able to communicate outside as well as people throughout the organisation. They are adept at getting others to agree to their private vision.
 9. Intrapreneurs are not large risk takers. Their major risk is in devoting so much time and commitment to their ideas.
 10. Intrapreneurs attempt to minimise organisational failure.
 11. Intrapreneurs do their own market research and intuitive market evaluation.
 12. Intrapreneurs are excellent decision makers. They are able to make decisions, often without enough data as they are very analytical.
-

Source: Cornwall & Perlman, 1990: 183.

3.4 THE STRATEGIC MANAGEMENT AND LEADERSHIP SKILLS NECESSARY TO BE A SUCCESSFUL ENTREPRENEURIAL FRANCHISOR.

Strategic management usually focuses on what an enterprise or new venture is trying to achieve in the long run and when and how this should be achieved. Strategic management is usually *not* associated with entrepreneurship. According to Van Aardt, Van Aardt & Bezuidenhout (2000: 113) this is a very short-sighted view of entrepreneurship and also of planning a new venture. Everything an entrepreneur does when starting a new venture must be directly linked to strategic management.

The strategic goal of any entrepreneur should be to deliver goods and services to customers that they will purchase and value, and to do it in such a way that the service rendered is better than that of the competition. Strategy is an important component of success. An entrepreneur who operates without a strategy will flounder in the market-place and eventually go out of business when more focused competitors are better able to meet the needs of customers. Without a strategy, entrepreneurs are likely to misallocate resources and fail to co-ordinate their actions (Van Aardt, Van Aardt & Bezuidenhout, 2000: 114).

According to Wright (1995: 48-63) the major reasons for failure of businesses are the following (in order of importance):

- poor management skills;
- poor record-keeping;
- poor money management;
- too little effort to market the business;
- poor planning;
- poor pricing practices;
- poor human resources management and

- the entrepreneur's inability to adapt to the changing demands of a business or the industry.

There is no doubt that the success of a franchisor in the franchise industry is determined by certain specific management and leadership skills. To be successful, the franchisor whether individual entrepreneur or successful organisation, must realise that entrepreneurship is not just the "creation of ideas". Entrepreneurship does not function alone, it must be approached from a strategic management perspective (Cornwall & Perlman, 1990: 19). Especially organisational entrepreneurship must be part of the broad strategic plans of an organisation. It must also be an integral part of the implementation of these plans. The five most important components or tasks according to Thompson & Strickland (1998: 3) are:

3.3.1 **Developing a strategic vision and business mission**

A company's *mission* is often termed "what" a company is currently seeking to do for its customer. But setting forth what a company is doing today or what it has done in the past doesn't speak for the future or incorporate a sense of needed change and long-term direction. This will ask for excellent and innovative know-how and skills to determine what a venture or a company will have to do to meet its customers needs tomorrow. Thus the franchisor as entrepreneur are obliged, even from the beginning, to look beyond the present business mission and think strategically about the impact of new technologies and opportunities on the horizon. This kind of view a company tries to create, and the kind of business position it wants to stake out in the years to come will constitute the *strategic vision* of the company. This vision will be particularly important to the entrepreneurial organisation, as it will provide the fuel to drive the innovative actions of employees within the corporation.

3.3.2 Setting objectives

The purpose of setting objectives is to convert managerial statements of strategic vision and business mission into specific performance targets. Two very distinctive types of performance targets are required:

Financial Objectives

- Growth in revenues
- Growth in earnings
- Higher dividends
- Wider profit margins
- Higher returns on invested capital
- Attractive economic value added (EVA) performance
- Strong bond and credit ratings
- Bigger cash flows
- A rising stock price
- Attractive and sustainable increases in market value added (MVA)
- Recognition as a “blue chip” company
- A more diversified revenue base
- Stable earnings during periods of recession

Strategic Objectives

- A bigger market share
- Quicker design-to-market times than rivals
- Higher product quality than rivals
- Lower costs relative to key competitors
- Broader or more attractive product line than rivals
- A stronger reputation with customers than rivals
- Superior customer service
- Recognition as a leader in technology and/or product innovation
- Wider geographic coverage than rivals
- Higher levels of customer satisfaction than rivals

Achieving acceptable financial performance is a must but achieving acceptable strategic performance is essential to sustaining and improving a company's long-term market position and competitiveness. The franchisor that consistently passes up opportunities to strengthen the franchise's long-term competitive position in order to realise better near-term financial gains risks diluting its competitiveness, losing momentum in its market, and impairing its ability to stave off market challenges from rivals.

Although the franchisor, due to the specific nature of its operations, will not be able to meet all objectives, those applicable must be clear and specific and it must set measurable targets within specified periods of time. Very important is that these objectives as goals, as well as the results thereof be communicated and shared with all stakeholders.

3.3.3 Crafting a strategy

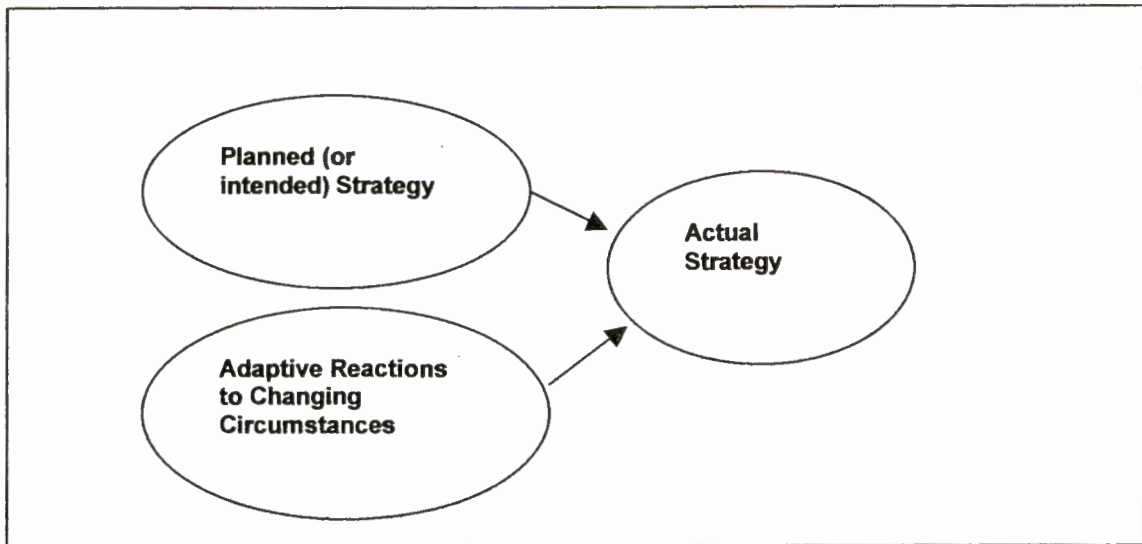
A company's strategy usually represents answers to the following important business issues:

- Whether to concentrate on a single business or to build a diversified group of businesses?
- Whether to create a broad range of customers or focus on a particular market niche?
- Whether to develop a wide or narrow product line?
- Which competitive strategy to pursue e.g. low cost versus product superiority?
- How big a geographic market to try to cover?
- How to react to new market and competitive conditions?
- How to grow the enterprise over the long-term?

Crafting a winning strategy needs to be a *top priority* managerial task in *every organisation*. There is also a definite compelling need for the franchisor to be *proactive* in shaping *how* business will be conducted

in the future. And in strategy-making all franchisors and stake holders must take prudent risks and exercise entrepreneurship.

Exhibit 3.5 Strategy is both proactive (intended) and reactive (adaptive)



Source: Thompson & Strickland, 1998: 9.

3.3.4 Implementing and executing the strategy

Managing the process of implementing and executing strategy is primarily a *hands-on, close-to-the scene administrative* task that includes the following principal aspects:

- Building an organisation capable of carrying out the strategy successfully.
- Developing budgets that steer resources into those internal activities critical to strategic success.
- Establishing strategy-supportive policies and operating procedures.
- Motivating people in ways that induce them to pursue the target objectives energetically and, if need be, modifying their duties and

job behavior to better fit the requirements of successful strategy execution.

- Trying the reward structure to the achievement of targeted results.
- Creating a company culture and work climate through entrepreneurship and intrapreneurship respectively which is conducive to successful strategy implementation and execution.
- Installing information, communication, and operating systems that enable company personnel to carry out their strategic roles effectively day in and day out.
- Instituting best practices and programs for continuous improvement.
- Exerting the internal leadership needed to drive implementation forward and to keep improving on how the strategy is being executed.

The aim to successfully implement a strategy must be to create strong “fits” internally as well as externally. For the franchisor as individual entrepreneur this task is probably the most complicated and time-consuming. The franchisor as entrepreneurial organisation or strong venture management team, do tend to be more successful due to shared responsibility and aligned commitment. Notwithstanding this challenge, successful implementation determines overall long-term success and growth.

3.3.5 Evaluating performance, monitoring new developments, and initiating corrective adjustments

It is management's duty to stay on top of the company's situation, deciding whether things are going well internally and monitoring outside developments closely. These crucial activities constitutes responsible franchising. Priorities include:

- Corrective action and adjustments regarding sub-performance.
- Adjustments towards important new external circumstance.
- Alteration of long-term direction if needed.

- Redefinement of the business
- Broadening or narrowing of the company's vision. It can also be radically revised!

Finally, according to Van Aardt, Van Aardt & Bezuidenhout (2000: 142) leading is probably the strategic management task that the entrepreneur should devote most of his/her time. Only through effective leadership will it be possible to execute these five tasks identified by Thompson & Strickland. Leading is a difficult and demanding task as the entrepreneur not only has to supervise strategy and activities, but also people. The entrepreneur will only grow and be successful if the entrepreneurial teams grows. This growth usually constitutes much organisation learning.

“Proficient strategy is always the product of much organisational learning” (Thompson & Strickland, 1998: 16). In the end it comes down to being informed, focused, flexible and adaptive. This is especially true in the case of the franchisor as entrepreneurial leader. Research has shown (Timmons, 1999: 228) that this organisational learning is usually the entrepreneur's apprenticeship and are often an integral part of the process of shaping an entrepreneurial career. See McDonald's strategy (Annexure A). In chapter 4, it will be determined if the most important strategic management and leadership skills has been acquired through this apprenticeship, and if it is utilised effectively in order to be conducive to responsible and ethical franchising.

CHAPTER 4

FIELD STUDY AND RESULTS

4.1 METHOD OF RESEARCH

The aim of this dissertation as mentioned, will be to compile a profile of the successful franchisor in the South African franchising industry. The assumption that the franchisor is or should be an entrepreneurial leader with certain important skills; as well as the most important criteria determining strategic management and leadership performance, have been used to determine this profile. The *successful franchisor*, in South Africa, is usually one of the following:

- an entrepreneurial individual who exercise the option of franchising, in order to expand a successful venture.
- an intrapreneur or team of intrapreneurs within big corporate companies, recognising a viable business opportunity.
- a team of entrepreneurs or partners with complementary skills and know-how recognising a viable business opportunity.

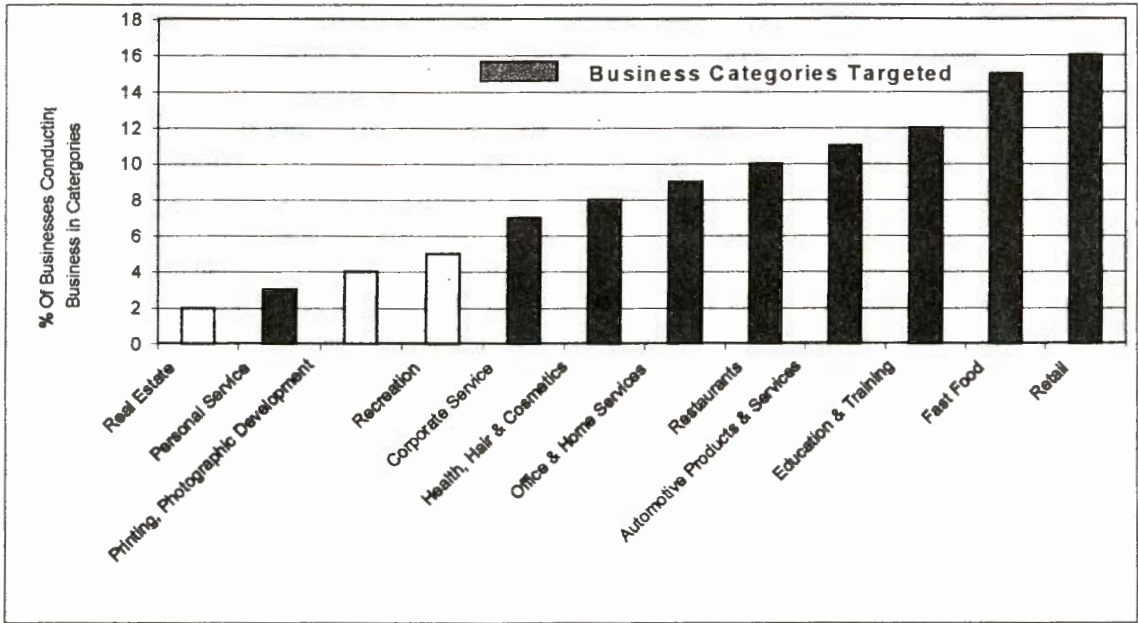
The method of research, in order to determine this profile, were by means of structured personal interview, questionnaire and follow-up telephonic discussion with 10 relatively well-know and successful franchisors operating within the South Africa franchise industry.

4.2 RESPONDENTS OF RESEARCH

Franchisors interviewed and chosen for research purposes were all representative of the three categories as mentioned on page 48. Together they represent more than a 1000 individual franchisees. These franchisors represent at least 9 out of the 12 business categories identified and used by Consulata for their research to determine the top-franchises in South Africa (see exhibit 4.1).

Information supplied by these 10 franchisors, and used for this dissertation was identified from the Consulata research, various issues from Succeed magazine as well as a few promising franchises identified by Lipkin & Parker (1999: 212– 245).

Exhibit 4.1 Franchise business categories



4.3 RESULTS OF FIELD STUDY

Open-ended questions conducted by means of structured interview and follow-up telephonic discussions brought to light the following important facts:

4.3.1 The franchisor as entrepreneurial leader

- The 10 Franchisors interviewed represent a total of 1157 franchised outlets (average = 116).
- The average age of the specific franchise concepts is between 7 and 8 years (7,5).
- 8 of the 10 franchisors are members of FASA.
- 7 of the 10 entrepreneurs are still involved in the operations of the venture.

- Just 4 franchisors benchmarked their ventures against other successful franchises (either in South Africa or abroad).
- Just 4 franchisors used a professional franchising consultant to develop their specific concept.
- 4 ventures operates as Public Companies whereas the remaining 6 are divisions or part of listed Holding Companies.
- 4 ventures franchised their concept from the very beginning.
- Just 4 franchisors do not make use of master franchisees. The remainder does, mainly in neighboring countries.
- All Franchisors interviewed share the opinion that the industry should be self-regulating and that government legislation would not necessarily solve the problems/challenges facing the industry.
- Of the 10 franchisors interviewed, at least 5 have received national recognition from bodies such as FASA and local Business Chambers. Recent (1996 - 2000) nominations and accolades include:
 - Brand Builder of the year Award (FASA)
 - Newcomer Franchiser of the year (FASA)
 - Leading Developer of Emerging Entrepreneurs (FASA)
 - Franchisor of the year (FASA)
 - Customer Service Excellence (Chamber/s of Business)
 - Best Business and Business/personality of the year (Chamber/s of Business).

4.3.2 Rating the importance of strategic management and leadership skills of the franchisor

According to Timmons (1999: 221) testimony given by entrepreneurs confirms certain *strategic management*, leadership and *administrative* skills that they have in common. In order to determine not only the existence but also the level and importance of such skills, a questionnaire was given to the 10 franchisors (see Annexures C & D). No weight was assigned to these skills as it is important to manage and have control over all these skills, no matter which industry or business category a specific franchisor operates in. Individual scores however, were accumulated and averaged. The results were:

(1 = least important, 5 or 8 eg. = very important)

1. COMMITMENT AND DETERMINATION (1-5)	
Discipline	4,4
Persistence	3,5
Willingness to undertake personal sacrifice	3,1
Decisiveness	2,7
Total immersion	1
2. LEADERSHIP (1-10)	
Integrity	8,2
Inspires others	7,1
Reliability	7
Team builder	6,7
Self starter	6,2
Learner and teacher	5,3
Sharing of wealth	4,9
Urgency	4,2
Patience	2,7
Hero maker	1,5
3. OPPORTUNITY OBSESSION (1-3)	
Knows customers needs	2,6
Market driven	2,1
Value creation	1,3
4. TOLERANCE OF RISK, AMBIGUITY AND UNCERTAINTY (1-6)	
Calculated risk taker	5,1
Manages paradoxes and contradictions	4,1
Tolerance of uncertainty	3,9
Risk sharer	3,3
Tolerance of stress and conflict	2,8
Risk minimizer	2,1
5. CREATIVITY, SELF-RELIANCE AND ABILITY TO ADAPT (1-5)	
Ability to adapt	4,5
Nonconventional, open minded	3,9
Ability to learn quickly	2,5
Lack of fear of failure	2,0
Ability to conceptualize and "sweet details"	1,8
6. MOTIVATION TO EXCEL (1-6)	
Goal-and-results orientated	5,1
Drive to achieve and grow	5,0
Interpersonally supporting	3,6
Aware of weaknesses and strengths	3,2
Low need for status and power	2,1
Having perspective and sense of humor	1,9

General management and administrative competencies

(1 = least important, 5 or 8 eg. = very important)

1.	ADMINISTRATOR (1-8)	
	Communicating	6,2
	Planning	5,8
	Negotiating	4,9
	Decision making	4,8
	Problem solving	4,7
	Personnel administration	3,7
	Project management	3,6
	Managing outside professionals	1,6
2.	LEGAL ISSUES (1-6)	
	Corporate and securities law	4,2
	Corporate law	4,0
	Bankruptcy law	3,9
	Law relating to patent and proprietary rights	3,7
	Tax law	3,3
	Real estate law	1,3
3.	MARKETING (1-9)	
	Marketing planning	7,4
	Market research and evaluation	5,7
	Service management	5,6
	Distribution management	5,6
	Sales management	5,1
	Product price	4,8
	Product management	4,3
	Direct selling	4,0
	New-product planning	3,8
4.	OPERATIONS/PRODUCTION (1-7)	
	Quality control	5,9
	Cost analysis and control	4,9
	Manufacturing management	4,8
	Inventory control	4,0
	Purchasing	3,5
	Production scheduling and flow	3,3
	Job evaluation	2,1
5.	FINANCE (1-6)	
	Managing cash flow	5,4
	Credit and collection management	4,0
	Bookkeeping, accounting and control	3,7
	Raising capital	3,6
	Short-term financing alternatives	2,3
	Public and private offerings	1,8
6.	TECHNICAL SKILLS (IT) (1-5)	
	Spreadsheet analysis	4,7
	Word processing etc.	3,9
	Electronic mail	2,5
	Web-site development	2,0
	Marketing through the Internet	1,9

4.3.3 Evaluation of results

Although all of these skills are important for the franchisor to achieve long-term success, not all franchisors found that they were or are skilled in the areas listed. Upon questioning however it was clear that even since initiation they realised this and made a deliberate attempt to acquire these skills, through apprenticeship, through partners or through the use of advisors. At least *three* ventures were initiated by chartered accountants. The venture was then further developed with a partner/s with relevant industry or technical skills. *Nine* franchisors interviewed were managed by highly competent teams with relevant formal managerial, as well as financial qualifications. Only *one* franchise however, had a highly qualified marketing specialist on the team, which probably explains the success in the highly competitive market they operate in. The remainder make use of external marketing consultants or agencies. Some only occasionally. *Three* ventures, lastly, were deliberate strategic attempts to distribute the ventures' products and services more cost-effectively by means of franchising. *Three* entrepreneurial ventures (franchises) were bought by holding companies therefore providing perfect strategic fit within their respective industries.

After strengths evaluating, analysing and comparing the above facts, the following strengths and weaknesses may be interpreted:

Strengths

- The depth of managerial and financial experience, expertise and practises.
- Acquiring or contracting the relevant technological and technical skills relevant to their respective industries.
- Importance attached to the customer through quality deliverance of service, quality of products and services delivered.

- The use of a skills complementary venture management team.
- Lean and flat top management structure.
- The majority of initial entrepreneurs are still active and involved as internal or external board directors.
- The support of a strong financial holding company minimizing the risk factor regarding decision making.
- The majority of franchisors were and still are more interested in creating more “slices of the pie” than having less slices, but bigger slices. This embodies true entrepreneurial spirit.
- The importance attached to organisational communication and negotiation as administrative tasks. Effective communication as skill is crucial as the operations of franchisors are usually decentralised.

Weaknesses

- Lack of entrepreneurship in certain areas probably due to the over-emphasis on performance. True entrepreneurs are obsessed with value creation and are not afraid to “sweat the details” (see low score).
- The majority of franchisors interviewed probably experience an average to low franchisor-franchisee relationship (see low score). True entrepreneurs are hero-makers, they regularly draw their top franchisees into their management teams and also use them on advisory councils. *Three* of the franchisors interviewed make use of this practise, which probably explain these ventures’ creativeness and success.
- The lack of a marketing specialist, manager or consultant within the venture. Notwithstanding the usual monthly advertising fees franchisees have to contribute to, very little attention is given to continued long-term strategic marketing. Just *two* of the ten franchisors interviewed were found to be “brand and marketing obsessed”, which also probably explain their respective successes.

- New product planning and development also received a low score, which is dangerous in the changing and volatile economic climate businesses currently have to operate in.
- It seems that none of the franchisors seem to realise the benefit of making use of e-commerce (see low score). The reason may probably be lack of knowledge or perceived unsuitability of the medium.
- Raising capital (see low rating), if only to assist franchisees and branch outlets, should also be given more attention. Franchising in the U.S.A. have gone this way some time ago, but only a few stronger franchisors in South Africa offer this benefit. The poor financial support and assistance in this regard from financial institutions are probably the major contributor to this weakness.

Regarding the above, it is safe to presume that these franchisors are strong for a number of reasons. Perhaps the most important is that they are uniform, disciplined and flexible. These reasons are also the result of highly competent experienced leaders and managers that have been active in their respective fields for considerable time. It is also clear that these 10 franchisors interviewed dispose and attach value to the applicable strategic management and leadership skills necessary in order to be successful entrepreneurial franchisors.

CHAPTER 5

CONCLUSION

5.1 EXERCISING FRANCHISING “DUE-DILLIGENCE”

Franchising in South Africa is going through difficult times. Quite a few solid companies that once had many successful franchised outlets have been publishing worse than expected results or have gone into liquidation.

The liquidations of O’Hagans, PNA and Boss Glass in 1999 were not entirely unexpected. They nevertheless sent shock waves through an industry that is feeling the effect of the difficult trading conditions prevailing at the moment. Drastically reduced profits from a number of other listed franchises have been interpreted as danger signals by some observers. There is no doubt that franchising, when practised correctly, has enormous benefits for a country like South Africa where skills levels are low. But there are things that need to be corrected – and the sooner they are, the better for the many excellent franchise companies operating in South Africa (Anon, 1999: 85).

Whereas certain franchise developers lay the blame with poor franchise selection, others blame the many naïve franchisors using franchising as a cheap and fast way to expansion. The substantial capital resources necessary to do the job properly are sadly lacking. These non performers are in fact more like product trade name franchises, and is not the way franchise companies should be run.

More than ever, also in South Africa, a franchise’s management team must know its customers. Customer and product research as well as focus is essential in today’s franchise-business field. Franchisors and franchisees should work together, promote the common good of the

venture. “The customer should be the real competition” (Haskell, 2000: 10). To thrive, franchisors and their franchisees must be *friendly, flexible, fast and focused*. Profits disappear when the customer fails to receive value. Franchisors are entrepreneurial leaders after all, which indicates that the creation of value should be assigned top priority.

Investors or would-be franchisees should not be embarrassed to put forward specific questions regarding the skills identified in the previous chapter. The types of questions to ask a potential franchisor include:

- Is there a demand in the market for the products/services? Make sure that the market demand is sizeable, sustainable and substantiated with legitimate sales and marketing statistics.
- Has the product/service got staying power? Does it possess “retain business” possibility? An idea or fad cannot be franchised, it doesn’t have long-term potential.
- What is the track record of the franchisor? A good franchisor has excellent references, happy franchisees and a good reputation in its specific industry.
- Is the franchisor of choice up to industry standards and benchmarks?
- Who is the competition and how strong are they? Does the prospective franchisor possess a sizeable slice of the cake?
- Franchisors interviewed emphatically stated that affiliation to FASA makes it easier to attract new franchisees. FASA membership, however, does not necessarily guarantee success. Visit a selection of franchisees and establish if they are happy with their investment.
- Is the franchisor prepared to show you the financial results of his company owned outlets? How many are there? Are they performing well?

Finally, franchisors normally fall into one of the following categories:

1. The excellent and established professional franchisor.

2. The franchisor of a promising but unproven concept.
3. The franchisor doomed for failure due to lack of experience, untried concept and who does not have a viable business product or service.

It is essential to avoid the third category. Category two do possess potential but may be risky and of speculative nature. Do not invest in category two until the concept has been piloted in various geographical areas for at least one year.

It does seem the safer option to invest in an established professional franchisor managed by an accomplished highly competent management team.

5.2 THE SUCCESSFUL FRANCHISOR IN THE SOUTH AFRICAN FRANCHISE INDUSTRY

In order to exercise proper “due diligence” this dissertation’s aim was to compile a profile of a successful franchisor in the South African franchise industry. In order to do this, specific strategic management, leadership and administrative skills of 10 top franchisors have been evaluated and analysed.

As support is vital to a franchisee, it should be provided by a solid experienced management team as well as competent knowledgeable support staff. This very often does not happen although promised and stipulated as such in the franchise agreement between franchisor and franchisee. This dissertation in particular has been an effort towards establishing if such experienced management teams and staff with supporting skills do indeed exist. And if they do, if the necessary skills are in place which are vital to long-term growth and success.

It is clear from this evaluation that criteria relevant to strategic management and leadership skills in the franchise industry are met

by the 10 franchisors interviewed. The most important strengths as well as weaknesses have been identified and the deduction can therefore be made that these franchisors do indeed dispose of the most important strategic management and leadership skills necessary to be successful entrepreneurial franchisors. The success of these franchises can be contributed to being managed by highly competent experienced entrepreneurial leaders and managers that have been active in their respective fields for considerable time.

The successful entrepreneurial franchisor in the South African franchising industry therefor value as well as dispose of the following important management and leadership skills and practises:

- sound managerial, financial and marketing expertise and experience
- a high priority is attached to the deliverance of quality service to all stakeholders; the customer, the franchisee as well as all employees
- definite entrepreneurial flair and creativity
- a high priority is assigned to integrity
- a high priority is assigned to reliability and dependability
- above average communication capabilities
- a high priority is assigned to innovation and adaptability conducive to successful intrapreneurship
- definite need to be goal and result orientated, however, strategic objectives are favoured over short-term financial gain
- a high priority is assigned to persistence and staying power
- the necessary know-how and ability to attract the relevant skills in order to stay competitive and entrepreneurial.

The *franchisor*, whether the individual entrepreneur or as experienced management team, is responsible for the success of its venture. *By having a strong capable management team with necessary skills in place a prospective investor or would-be franchisee can be assured of the intent of such a franchisor.*

BIBLIOGRAPHY

ANON. 1995. Franchising : look before you leap. *Finance Week*, 65. (7) : 5 -6, May.

ANON. 1999. The state of franchising today. *Succeed*. 82-85, Aug/Sept.

ANON. 2000. Unlocking potential. *Succeed*. 24, Apr/May.

ANON. 2000. Franchising in South Africa. *Succeed*. 66-68, Feb/Mrch.

BARROW, C. & GOLZEN, G. 1991. Taking up a Franchise. 8th ed. London : Kogan Page.

CORNWALL, G. R. & PERLMAN, B. 1990. Organizational Entrepreneurship. Homewood : Irwin.

COVEY, S. 2000. The four roles of a leader. *Succeed*. 26-27, Aug/Sept.

DEARLOVE, D. 1999. Business the Bill Gates Way. Oxford: Capstone Publishing Limited.

EBERSON, W. 1991. The Ethics of Franchising. *Succeed*. 23-34, Oct/Nov.

FASA. 2000. Ethical Franchising : Franchising the wave of the future. 1-9.

FICK, C. C. 1998. 'n Evaluasie van die Franchise konsep vanuit 'n regsoogpunt. Potchefstroom.

HASKELL, C. B. 1996. Franchisors: Just who are your Customers, Anyhow? *Franchising World*, 23. (3) : 9 – 11, May/June.

KREITNER, R. & KINICKI, A. 1998. *Organizational Behavior*. 4th ed. Boston: Irwin Mc Graw-Hill.

LIPKIN, M. & PARKER, E. *You're the Boss!! How to grow rich by working for yourself*. 1999. Johannesburg : Touch The Sky Publishers.

MITTNER, M. & VAN DER WALT, T. D. 1998. Unleashing the entrepreneurial spirit. *Finance Week*. 49 – 50, Nov. 20.

MOROBÉ, D. 1991. On your own : due diligence. *People dynamics*, 17. (11) : 94 – 95, Nov/Dec.

NAUDE, C. 2000. S.A. se top-franchises. *Bylae tot Finansies & Tegniek*. 3-14, 12 Mei.

SCHULTZ, R. 1999. Franchisors, Franchisees must work together to flourish. *Hotel and Motel Management*, 214 . (19) : 1-2, Jan.

SHEPHARD, G. J. 1999. Success Depends on Understanding Franchisee/ Franchisor Relationship. *Business First – Columbus*, 16. (1) : Mrch.

STONE, A. 2000. Do your homework before buying a franchise. *Succeed*. 52-53, Apr/May.

STONE. A. 2000. Building Trust – the role of the Franchising Association of SA. *Succeed*. 46-50, Apr/May.

THOMPSON, A. A. & STRICKLAND, A. J. 1998. *Strategic Management : Concepts and Cases*. 10th ed. Boston : Irwin McGraw-Hill.

TIMMONS, J. A. *New Venture Creation : Entrepreneurship for the 21st Century*. 5th ed. Boston: Irwin Mc Graw-Hill.

VAN AARDT, I., VAN AARDT, C. & BEZUIDENHOUT, S. 2000
Entrepreneurship and New Venture Management. 2nd ed. Oxford: Oxford
University Press.

VENTER, J. 1999. The saddest franchise stories - In the public interest.
Succeed. 18-23, Aug/Sept.

WILKERSON, J. 1999. Franchisors need not to be pioneers to be
successful : Franchisee Relationships prove more important. *Nation's
Restaurant News*, 33. (43) : 3-4, Oct.

WRIGHT, C. 1995. Successful small business management in South Africa:
Choosing a small business, starting a business, raising capital, avoiding
pitfalls, running your business. Wynberg: Struik.

ANNEXURE A

1. THE DISCLOSURE DOCUMENT – Disclosure General

- 1.1** All franchisors or prospective franchisors will be required to provide disclosure by way of a Disclosure Document which complies with the provisions of the FASA Code of Ethics. The disclosure document will be revised and updated not less frequently than once in any 12 calendar month period.
- 1.2** The Disclosure Document together with a copy of the franchise agreement will be provided to all prospective franchisees at least seven days prior to the entering into of any franchise or other binding agreement or the payment of any monies by the franchisee. A Disclosure Document must be provided to existing franchisees not less than 3 months before the renewal of any franchise agreement.
- 1.3** The Disclosure Document may be enhanced by a codicil giving additional information applicable to any particular franchise outlet e.g. specific rental provisions, franchisor head-lease, master licence information and so on.
- 1.4** The Disclosure Document must be accompanied by an auditor's certificate, certifying that the business of the franchisor is a going concern.
- 1.5** A franchisor may elaborate on the financial position of the franchisor's business or its structure, e.g. where the franchisor company is part of a group of companies or a

subsidiary of a holding company, or a joint venture partner and so on.

- 1.6 Where a franchisor and a master sub-franchisor are party to a contract with a franchisee, the Disclosure Document will contain material information in relation to both the franchisor and the master sub franchisor, including auditor's certificates relating to both the franchisor and the master sub-franchisor.

Where the franchisor is not a party to a contract with the franchisee and the franchise agreement is a two-party agreement between the master sub-francisor and the franchisee, the Disclosure Document need only contain information relating to the master sub-franchisor and the franchise system generally.

2. DISCLOSURE DOCUMENT REQUIREMENT

- 2.1 The Disclosure Document will be in English or Afrikaans and a written explanation will be given of any terms or sections not fully understood by the franchisee.
- 2.2 Legal name and trading name of the franchisor, registered office and franchise business office of the franchisor. In both cases, street address, postal address, telephone and fax numbers must be shown. State if the franchisor is a member of the Franchise Association of Southern Africa.
- 2.3 the franchisor and his officers. (The term "officers" will include all relevant major shareholders, members, directors and executive officers).

2.4 A résumé of the business experience of the franchisor and his officers, including

2.4.1 length of experience in the type of business offered in the franchise;

2.4.2 length of experience in operating or offering the franchise; and

2.4.3 length of experience in operating or offering other franchises and a description of those franchises.

2.5 Viability statement with key financial information in respect of the franchisor from the franchisor's directors/principals.

2.6 Details of any material debt, criminal, civil or administrative proceeding in which the franchisor was cited as the defendant, respondent or accused, during the past five years, calculated from the date the Disclosure Document was updated.

2.7 Summary of the main particulars and features of the franchise, including:

2.7.1 nature and period of existence of the franchise system and how it has developed;

2.7.2 examples of any trade mark, logo, symbol etc., used by the franchisor and steps taken to protect these and

details of any threatened or pending litigation in relation to them;

2.7.3 details of payments to be made by the franchisee to the franchisor (including method of calculation if applicable);

2.7.4 particulars of any restrictions (eg. territorial) imposed on the franchisee;

2.7.5 basis of franchisor's involvement / approval for site selection;

2.7.6 summary of terms and conditions relating to termination, renewal, goodwill and assignment of the franchise;

2.7.7 summary of the main obligations of the franchisor (including initial and ongoing training to be provided).

2.8 Whilst the franchisor shall not be obliged to deliver the Operations Manual or any other procedural document prior to the finalising of the franchise agreement, the document must be shown to the franchisee.

2.9 A tabulated list of components making up the franchise purchase e.g. franchise fee, stock, fixtures/fittings, working capital etc, with (estimated) individual cost totalled to reflect the full outlay. A summary of those items which could be

leased and (estimated) costs involved – being part of the full outlay.

See Sections 4 and 5.

- 2.10 Details of any financial requirements by the franchisor of the franchisee, e.g. specific amount of the franchisee's own contribution towards the franchise purchase price.
- 2.11 The number of existing franchisees (including address and telephone number of each and year commenced business) should be available for referee purposes. Should a full list be impractical, then a list of franchisees in the province should be provided. Number of franchises terminated or not renewed, over the past year. Details of any current unresolved litigation with any existing or former franchisees.
- 2.12 Projections
 - 2.12.1 Where written projections are provided in respect of levels of potential sales, income, gross/net profits or other financial projections etc. for the franchise or franchises of a similar nature, particulars of the basis/assumptions upon which the representations are made shall be provided.
 - 2.12.2 Each page of the projections should be qualified in respect of such basis/assumptions, for example:
These figures represent ACTUAL performance by either the franchisor (or a franchisee). There is no guarantee that you will achieve these figures and nor

BIBLIOGRAPHY

- ANON. 1995. Franchising : look before you leap. *Finance Week*, 65. (7) : 5 -6, May.
- ANON. 1999. The state of franchising today. *Succeed*. 82-85, Aug/Sept.
- ANON. 2000. Unlocking potential. *Succeed*. 24, Apr/May.
- ANON. 2000. Franchising in South Africa. *Succeed*. 66-68, Feb/Mrch.
- BARROW, C. & GOLZEN, G. 1991. Taking up a Franchise. 8th ed. London : Kogan Page.
- CORNWALL, G. R. & PERLMAN, B. 1990. Organizational Entrepreneurship. Homewood : Irwin.
- COVEY, S. 2000. The four roles of a leader. *Succeed*. 26-27, Aug/Sept.
- DEARLOVE, D. 1999. Business the Bill Gates Way. Oxford: Capstone Publishing Limited.
- EBERSOHN, W. 1991. The Ethics of Franchising. *Succeed*. 23–34, Oct/Nov.
- FASA. 2000. Ethical Franchising : Franchising the wave of the future. 1-9.
- FICK, C. C. 1998. 'n Evaluasie van die Franchise konsep vanuit 'n regsoogpunt. Potchefstroom.
- HASKELL, C. B. 1996. Franchisors: Just who are your Customers, Anyhow? *Franchising World*, 23. (3) : 9 – 11, May/June.

KREITNER, R. & KINICKI, A. 1998. Organizational Behavior. 4th ed. Boston: Irwin Mc Graw-Hill.

LIPKIN, M. & PARKER, E. You're the Boss!! How to grow rich by working for yourself. 1999. Johannesburg : Touch The Sky Publishers.

MITTNER, M. & VAN DER WALT, T. D. 1998. Unleashing the entrepreneurial spirit. *Finance Week*. 49 – 50, Nov. 20.

MOROBÉ, D. 1991. On your own : due diligence. *People dynamics*, 17. (11) : 94 – 95, Nov/Dec.

NAUDE, C. 2000. S.A. se top-franchises. *Bylaë tot Finansies & Tegniek*. 3-14, 12 Mei.

SCHULTZ, R. 1999. Franchisors, Franchisees must work together to flourish. *Hotel and Motel Management*, 214 . (19) : 1-2, Jan.

SHEPHARD, G. J. 1999. Success Depends on Understanding Franchisee/ Franchisor Relationship. *Business First – Columbus*, 16. (1) : Mrch.

STONE, A. 2000. Do your homework before buying a franchise. *Succeed*. 52-53, Apr/May.

STONE. A. 2000. Building Trust – the role of the Franchising Association of SA. *Succeed*. 46-50, Apr/May.

THOMPSON, A. A. & STRICKLAND, A. J. 1998. Strategic Management : Concepts and Cases. 10th ed. Boston : Irwin McGraw-Hill.

TIMMONS, J. A. New Venture Creation : Entrepreneurship for the 21st Century. 5th ed. Boston: Irwin Mc Graw-Hill.

VAN AARDT, I., VAN AARDT, C. & BEZUIDENHOUT, S. 2000
Entrepreneurship and New Venture Management. 2nd ed. Oxford: Oxford
University Press.

VENTER, J. 1999. The saddest franchise stories - In the public interest.
Succeed. 18-23, Aug/Sept.

WILKERSON, J. 1999. Franchisors need not to be pioneers to be
successful : Franchisee Relationships prove more important. *Nation's
Restaurant News*, 33. (43) : 3-4, Oct.

WRIGHT, C. 1995. Successful small business management in South Africa:
Choosing a small business, starting a business, raising capital, avoiding
pitfalls, running your business. Wynberg: Struik.

ANNEXURE A

1. THE DISCLOSURE DOCUMENT – Disclosure General

- 1.1 All franchisors or prospective franchisors will be required to provide disclosure by way of a Disclosure Document which complies with the provisions of the FASA Code of Ethics. The disclosure document will be revised and updated not less frequently than once in any 12 calendar month period.
- 1.2 The Disclosure Document together with a copy of the franchise agreement will be provided to all prospective franchisees at least seven days prior to the entering into of any franchise or other binding agreement or the payment of any monies by the franchisee. A Disclosure Document must be provided to existing franchisees not less than 3 months before the renewal of any franchise agreement.
- 1.3 The Disclosure Document may be enhanced by a codicil giving additional information applicable to any particular franchise outlet e.g. specific rental provisions, franchisor head-lease, master licence information and so on.
- 1.4 The Disclosure Document must be accompanied by an auditor's certificate, certifying that the business of the franchisor is a going concern.
- 1.5 A franchisor may elaborate on the financial position of the franchisor's business or its structure, e.g. where the franchisor company is part of a group of companies or a

subsidiary of a holding company, or a joint venture partner and so on.

- 1.6 Where a franchisor and a master sub-franchisor are party to a contract with a franchisee, the Disclosure Document will contain material information in relation to both the franchisor and the master sub franchisor, including auditor's certificates relating to both the franchisor and the master sub-franchisor.

Where the franchisor is not a party to a contract with the franchisee and the franchise agreement is a two-party agreement between the master sub-francisor and the franchisee, the Disclosure Document need only contain information relating to the master sub-franchisor and the franchise system generally.

2. DISCLOSURE DOCUMENT REQUIREMENT

- 2.1 The Disclosure Document will be in English or Afrikaans and a written explanation will be given of any terms or sections not fully understood by the franchisee.
- 2.2 Legal name and trading name of the franchisor, registered office and franchise business office of the franchisor. In both cases, street address, postal address, telephone and fax numbers must be shown. State if the franchisor is a member of the Franchise Association of Southern Africa.
- 2.3 the franchisor and his officers. (The term "officers" will include all relevant major shareholders, members, directors and executive officers).

2.4 A résumé of the business experience of the franchisor and his officers, including

2.4.1 length of experience in the type of business offered in the franchise;

2.4.2 length of experience in operating or offering the franchise; and

2.4.3 length of experience in operating or offering other franchises and a description of those franchises.

2.5 Viability statement with key financial information in respect of the franchisor from the franchisor's directors/principals.

2.6 Details of any material debt, criminal, civil or administrative proceeding in which the franchisor was cited as the defendant, respondent or accused, during the past five years, calculated from the date the Disclosure Document was updated.

2.7 Summary of the main particulars and features of the franchise, including:

2.7.1 nature and period of existence of the franchise system and how it has developed;

2.7.2 examples of any trade mark, logo, symbol etc., used by the franchisor and steps taken to protect these and

details of any threatened or pending litigation in relation to them;

2.7.3 details of payments to be made by the franchisee to the franchisor (including method of calculation if applicable);

2.7.4 particulars of any restrictions (eg. territorial) imposed on the franchisee;

2.7.5 basis of franchisor's involvement / approval for site selection;

2.7.6 summary of terms and conditions relating to termination, renewal, goodwill and assignment of the franchise;

2.7.7 summary of the main obligations of the franchisor (including initial and ongoing training to be provided).

2.8 Whilst the franchisor shall not be obliged to deliver the Operations Manual or any other procedural document prior to the finalising of the franchise agreement, the document must be shown to the franchisee.

2.9 A tabulated list of components making up the franchise purchase e.g. franchise fee, stock, fixtures/fittings, working capital etc, with (estimated) individual cost totalled to reflect the full outlay. A summary of those items which could be

leased and (estimated) costs involved – being part of the full outlay.

See Sections 4 and 5.

2.10 Details of any financial requirements by the franchisor of the franchisee, e.g. specific amount of the franchisee's own contribution towards the franchise purchase price.

2.11 The number of existing franchisees (including address and telephone number of each and year commenced business) should be available for referee purposes. Should a full list be impractical, then a list of franchisees in the province should be provided. Number of franchises terminated or not renewed, over the past year. Details of any current unresolved litigation with any existing or former franchisees.

2.12 Projections

2.12.1 Where written projections are provided in respect of levels of potential sales, income, gross/net profits or other financial projections etc. for the franchise or franchises of a similar nature, particulars of the basis/assumptions upon which the representations are made shall be provided.

2.12.2 Each page of the projections should be qualified in respect of such basis/assumptions, for example:
These figures represent ACTUAL performance by either the franchisor (or a franchisee). There is no guarantee that you will achieve these figures and nor

is it intended that you should relay on them as a guarantee.

OR

These figures indicate the gross profit margins and revenue expenses at stated turnover levels which have been experienced by (the franchisor in its own operations) or (the franchisees on average in the last profit and loss accounts which have been supplied to the franchisor).

There is no guarantee that you will achieve the same results, nor is it intended that you should relay on them as a guarantee.

2.12.3 A statement as to whether the territory or site to be franchised has been subject to any trading activity, particularly a previous franchise, and if so, the history and details including the circumstances of any cessation of the franchise.

2.13 The following statement will appear:
“This Disclosure Document should help you make up your mind. While it includes some information about your contract (franchise agreement), don’t relay on it alone to understand your contract. Read all of your contract carefully. Buying a franchise is a serious undertaking. Take your time to decide. It is recommended that you have the contract explained to you by an attorney and you should seek accountancy and financial advice on the franchise proposition.

For the calendar year 199X,..... (name of franchisor) is a member in good standing of the Franchise

Association of Southern Africa and if required, further information on this membership can be obtained from:

The Executive Director,
Franchise Association of Southern Africa
Postnet Suite 267
Private Bag X30500
Houghton
2041 Republic of South Africa

3. CERTIFICATION AND COOLING-OFF PERIOD

3.1 Prior to the execution of a franchise agreement, the franchisor will ensure that the franchisee received:

3.1.1 the Disclosure Document and the franchise agreement at least seven days prior to the signing of the franchise agreement or any other binding document;

3.1.2 "How to Evaluate a Franchise" (FASA):
and

3.1.3 a copy of the FASA Code of Ethics and Business Practices and has read them.

3.2 No franchise agreement may be signed earlier than the eight calendar day after the franchisee has signed a receipt for the Disclosure Document and the franchise agreement.

4. FINANCIAL OBLIGATIONS

The franchisor must provide a full assessment of the financial obligations of the franchisee in terms of the financial agreement. Inter alia:

4.1 The Initial Fee (IF) – payable to the franchisor on the signing of the franchise agreement. The franchisor should indicate the purpose of the fee eg.

- ◆ Access to intellectual property
- ◆ Cost of training
- ◆ Legal and financial charges
- ◆ Profit for the franchisor

4.2 ESTABLISHMENT COST (EC)

The franchisor must inform the prospective franchisee of the funds required to establish the business, e.g.

- ◆ Purchase or lease of property
- ◆ Site conversion costs
- ◆ Décor and signage
- ◆ Equipment
- ◆ Furniture
- ◆ Hiring and training of staff
- ◆ Opening stocks
- ◆ Legal and financial charges

and so on.

Some of these costs depend on the site chosen and cannot be quoted accurately in advance. However, upper and lower levels should be quoted in the initial negotiations.

4.3 INITIAL WORKING CAPITAL (IWC)

The basis for calculating the IWC must be clearly shown.

4.4 TOTAL INVESTMENT (TI)

The TI will include:

- ◆ Upfront fee
- ◆ Establishment costs
- ◆ Initial working capital

Any other funds required must be clearly stated.

4.5 INVESTMENT BEFORE BORROWINGS (IBB)

The total funds that the franchisee must invest before borrowing must be stated.

4.6 FRANCHISOR FUNDING (FF)

If funding is available from the franchisor then the level of the funding and the applicable conditions must be shown.

4.7 ONGOING PAYMENTS (OP)

4.7.1 Details must be given of the ongoing payments payable to the franchisor – eg.

- ◆ Are the “payments” fixed or variable – as below?
- ◆ Are all or part of the payments built in to the cost of goods or services that must be purchased from the franchisor?
- ◆ Stage at which the “payments” fall due (eg. three months after trading by the franchisee commences)

4.7.2 Variable “payments” based on a percentage of turnover can include

- ◆ Management Service Fee (MSF)

The services that the franchisee can expect in return for the MSF must be indicated.

- ◆ Contribution to Advertising and Marketing Fund (ADV)

It should be indicated:

- ◆ What types of ADV services can be expected?
- ◆ Is local advertising and marketing paid from this fund?
- ◆ Can franchisees participate in the decision making on ADV matters?

4.8 FINANCIAL CERTIFICATE

The franchisor will supply to the prospective franchisee a current auditor's certificate, certifying that the business of the franchisor is a going concern.

4.8.1 GROUP COMPANIES ONLY

- ◆ State ultimate parent company by name and country of incorporation (if applicable).
- ◆ List subsidiary companies by name, country of incorporation and percentage ownership (if applicable).

4.8.2 STATEMENT

We certify that there have been no significant material changes in the Company's financial position since the date of the auditor's certificate and the Company has reasonable grounds to believe that it will be able to pay its debts as and when they fall due.

Dated and signed by a duly authorised officer of the Company.

ANNEXURE B

In 1997 McDonald's was the leading food service retailer in the global consumer marketplace, with a strong brand name and systemwide restaurant sales approaching \$35. Two-thirds of its 22,000-plus restaurants were franchised to nearly 5,000 owner/operators around the world. Sales had grown an average of 6 percent in the United States and 20 percent outside the United States over the past 10 years. McDonald's food quality specifications, equipment technology, marketing and training programs, operating systems, site selection techniques, and supply systems were considered industry standards throughout the world. The company's strategic priorities were continued growth, providing exceptional customer care, remaining an efficient and quality producer, offering high value and good-tasting products, and effectively marketing McDonald's brand on a global scale. McDonald's strategy had eight core elements:

Growth Strategy

- Penetrate the market not currently served by adding 2,500 restaurants annually (an average of 8 per day), some company-owned and some franchised, with about two-thirds outside the United States. Establish a leading market position in foreign countries ahead of competitors.
- Promote more frequent customer visits via the addition of attractive menu items, low-price specials, Extra Value Meals, and children's play areas.

Franchising Strategy

- Grant franchises only to highly motivated, talented entrepreneurs with integrity and business experience and train them to become active, on-premise owners of McDonald's (no franchises were granted to corporations, partnerships, or passive investors).

Store Location and Construction Strategy

- Locate restaurants on sites offering convenience to customers and profitable growth potential. The company's research indicated that 70 percent of all decisions to eat at McDonald's were made on the spur of the moment, so its goal was to pick locations that were as convenient as possible for customers to visit. In the United States, the company supplemented its traditional suburban and urban locations with satellite outlets in food courts, airports, hospitals, universities, large shopping establishments (Wal-Mart, The Home Depot), and service stations; outside the United States, the strategy was to establish an initial presence in center cities, then open freestanding units with drive-thrus outside center cities.
- Reduce site costs and building costs by using standardized, cost-efficient store designs and by consolidating purchases of equipment and materials via a global sourcing system.
- Make sure restaurants are attractive and pleasing inside and out and, where feasible, provide drive-thru service and play areas for children.

Product Line Strategy

- Offer a limited menu.
- Improve the taste appeal of the items offered (especially sandwich selections).
Expand product offerings into new categories of fast food (chicken, Mexican, pizza, adult-oriented sandwiches, and so on) and include Source: more items for health-conscious customers.
- Do extensive testing to ensure consistent high quality and ample customer appeal before rolling out new menu items systemwide.

Store Operation

- Enforce stringent standards regarding food quality, store and equipment cleanliness, restaurant operating procedures, and friendly, courteous counter service.
- Develop new equipment and production systems that improve the ability to serve hotter, better-tasting food, faster and with greater accuracy.

Sales Promotion, Marketing, and Merchandising

- Enhance the McDonald's image of quality, service, cleanliness, and value globally via heavy media advertising and in-store merchandise promotions funded with fees tied to a percent of sales revenues at each restaurant.
- Use Ronald McDonald to create greater brand awareness among children and the Mc prefix to reinforce the connection of menu items and McDonald's.
- Project an attitude of happiness and interest in children.

Human Resources and Training

- Offer wage rates that are equitable and nondiscriminatory in every location; teach job skills; reward both individual and team performance; create career opportunities; have flexible work hours for student employees.
- Hire restaurant crews with good work habits and courteous attitudes and train them to act in ways that will impress customers; promote promising employees quickly
- Provide proper training on delivering customer satisfaction and running a fast-food business to franchisees, restaurant managers, and assistant managers. (Instructors at Hamburger University campuses in Illinois, Germany, England, Australia, and Japan annually train over 5,000 students in 22 languages.)

Social Responsibility and Community Citizenship

- Take an active community role-support local charities and community projects; help create a neighborhood spirit; promote education excellence.
- Sponsor Ronald McDonald Houses (at year-end 1995, there were 168 houses in 12 countries providing a home-away-from-home for families of seriously ill children receiving treatment at nearby hospitals.
- Promote workforce diversity, voluntary affirmative action, and minority-owned franchises (over 25 % of McDonald's franchisees were females and minorities).
- Adopt and encourage environmentally friendly practices.
- Provide nutritional information on McDonald's products to customers.

ANNEXURE C

STRATEGIC MANAGEMENT AND LEADERSHIP SKILLS

(1 = least important, 5 or 8 eg. = very important)

1. COMMITMENT AND DETERMINATION (1-5)

Persistence

Discipline

Decisiveness

Willingness to undertake personal sacrifice

Total immersion
2. LEADERSHIP (1-10)

Team builder

Hero maker

Self starter

Inspires others

Sharing of wealth

Integrity

Reliability
3. OPPORTUNITY OBSESSION (1-3)

Knows customers needs

Market driven

Value creation
4. TOLERANCE OF RISK, AMBIGUITY AND
UNCERTAINTY (1-6)

Calculated risk taker

Risk minimizer

Risk sharer

Manages paradoxes and contradictions

Tolerance of uncertainty

Tolerance of stress and conflict
5. CREATIVITY, SELF-RELIANCE AND ABILITY
TO ADAPT (1-5)

Nonconventional, open minded

Ability to adapt and change

Ability to learn quickly

Lack of fear of failure

Ability to conceptualize and "sweet details"
6. MOTIVATION TO EXCEL (1-6)

Goal-and-results orientated

Drive to achieve and grow

Low need for status and power

Interpersonally supporting

Aware of weaknesses and strengths

Having perspective and sense of humor

ANNEXURE D

GENERAL MANAGEMENT AND ADMINISTRATIVE COMPETENCIES

(1 = least important, 5 or 8 eg. = very important)

1. ADMINISTRATOR (1-8)

Problem solving

Communicating

Planning

Decision Making

Project Management

Negotiating

Managing outside professionals

Personnel administration
2. LEGAL ISSUES (1-6)

Corporate and securities law

Corporate law

Law relating to patent and proprietary rights

Tax law

Real estate law

Bankruptcy law
3. MARKETING (1-9)

Market research and evaluation

Marketing planning

Product pricing

Sales management

Direct selling

Service management

Distribution management

Product management

New-product planning
4. OPERATIONS/PRODUCTION (1-7)

Manufacturing management

Inventory control

Cost analysis and control

Quality control

Production scheduling and flow

Purchasing

Job evaluation
5. FINANCE (1-6)

Raising capital

Managing cash flow

Credit and collection management

Short-term financing alternatives

Public and private offerings

Bookkeeping, accounting and control

6. **TECHNICAL SKILLS (IT) (1-5)**

Spreadsheet analysis

Word processing etc.

Electronic mail

Web-site development

Marketing through the Internet
