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Foreign franchisor entry into developing countries: Influences on entry choices and economic growth
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Foreign Franchisor Entry into Developing Countries: Influences on Entry Choices and Economic Growth

Gary J. Castrogiovanni
George S. Vozikis

The research presented in this article contends that independent businessownership in developing countries can be assisted, but this may be too great of an initial step for prospective businessowners accustomed to traditional employment roles. Franchise acquisition often is a more viable alternative. Through franchising, individuals can acquire needed business skills and experience, which then could be diffused to nonfranchise sectors of the economy. Within this line of argument, propositions are offered and policy implications are described.

In many developing countries, wealth and power have been concentrated in the hands of small groups for several generations or even centuries (Hofstede 1997). Thus, the general populace, for the most part, often has little experience at starting and developing business enterprises, and very few know how to compete in relatively free markets. In efforts to assist developing countries, questions arise as to how the requisite human capital should be developed. Although would-be entrepreneurs could acquire some basic concepts and skills through educational efforts, they still would lack the experience and social networks needed to achieve superior business performance (Castrogiovanni 1996; Cooper, Gimeno-Gascon, and Woo 1994; Robinson 1982). In addition, they may not have the work ethic, risk tolerance, and other personality traits associated with entrepreneurial success (Hisrich and Peters 1989).

Franchising can address these problems because a new franchisee can draw from the experience of the franchisor and other franchisees in the existing franchise network. Through franchising, a prospective businessowner can gain a proven business system, upfront training, and ongoing support. Thus, franchise acquisition is often an easier and less risky route to businessownership than independent business start-up. Consequently, franchising can help foster widespread businessownership in developing countries where ownership and wealth have historically been concentrated in the hands of very few individuals. Furthermore, the business knowledge and skill gained through franchising would subsequently be diffused throughout nonfranchise sectors of the economy as current and former franchisees embark on new entrepreneurial ventures.

To date, however, franchising's potential contribution to economic growth has largely been unrealized in developing countries. Where foreign franchisors have entered such markets, they have tended to establishing firm-owned units, or sell franchises to foreign investors instead of prospective businessowners within the local populace. McDonald's provides a good example.

Prospective McDonald's franchisees must have access to capital in excess of $1 million. Then, they are placed on a waiting list for new franchise opportunities. When they reach the top of that list, they must be prepared to relocate and establish a new franchise wherever the particular opportunity arises. Otherwise, they forfeit the opportunity and are moved back to the bottom of the waiting list.

In developing countries, most prospective franchisees would not have access to sufficient capital to qualify for McDonald's' waiting list. Among the very few who would qualify, the chances are very slim that an opportunity within their home country would materialize at the same time that they reach the top of the list. Consequently, very few McDonald's franchisees in developing countries are drawn from the local populace. Thus, prospective businessowners among the local populace are unlikely to gain business training and experience as McDonald's franchisees.

The purpose of this article is to show how franchising can be used as a tool by government policy-makers seeking to foster economic growth in developing countries. The article examines relationships among economic forces viewed at three levels of abstraction—(1) environment level, (2) network level, and (3) individual level—to clarify the conditions under which franchising is likely to contribute to economic development. The article concludes by presenting suggestions for policy-makers seeking to tap the economic development potential of the franchising form of business.

Franchising arrangements have often been classified as either business-format franchising or licensing arrangements (see for example, Castrogiovanni and Justis 1998). This article focuses on business-format franchising, where the franchisor typically provides a relatively complete business concept, including detailed sets of administrative and operating procedures, because that is the type of franchising arrangement under which prospective businessowners tend to receive the most business training and support. The article further examines the entry of foreign franchisors into developing markets because it is through foreign entry that skills and experience are most directly imported to those markets. In addition, tendencies have been for fran-

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chising to first emerge in developing countries through the entry of foreign franchisors, with a domestic franchising sector developing later (Justis and Judd 1998). In this article, the term "franchisor" refers to a network of franchised and firm-owned units headquartered in a developed country, and the term "franchisee" refers to a person or group who contracts with a franchisor to establish one or more new units within a particular market.

Three Levels of Abstraction

Exhibit 1 illustrates the overarching conceptual perspective taken here. Environmental conditions influence franchisor decisions to enter a particular developing country. Network factors, some of which stem from the environmental conditions themselves, in turn influence franchisor decisions regarding the character of the network (e.g., franchised to total units; local to nonlocal franchisees) in the particular country. At the individual level, franchisees then influence environmental conditions to the extent that their business training and experience adds to the aggregate skill base of the population.

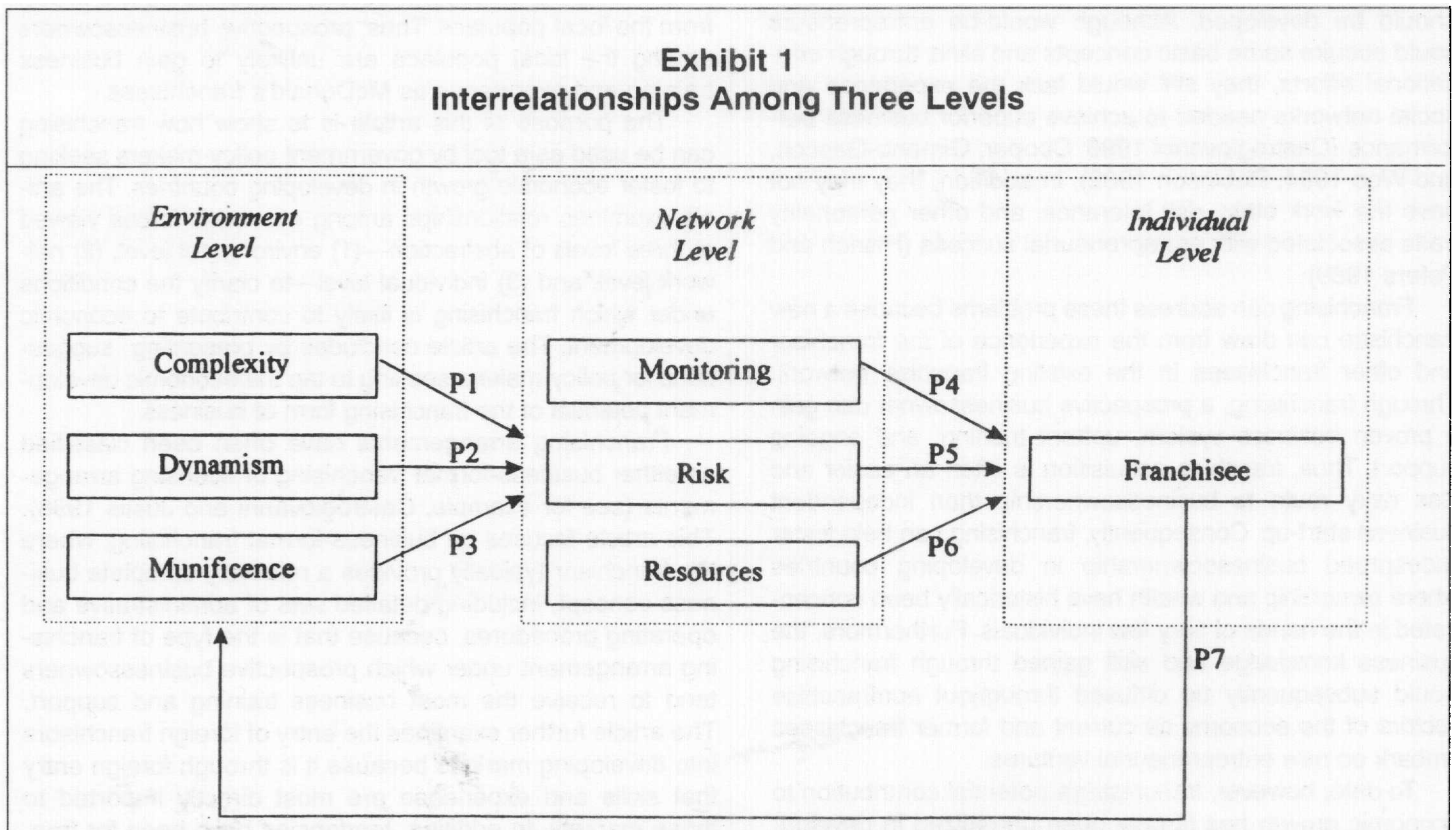
In Exhibit 1, "P1" through "P7" refer to sets of related propositions concerning relationships among the three levels. The first three sets of propositions (i.e., P1 – P3) are grounded in the organization environment, foreign entry, and franchise expansion literatures. The next four sets (P4 – P7) are grounded in the franchising strategy and structure literatures. Most propositions within those sets, however, are largely untested in studies of franchisor foreign entry. Nevertheless, the researchers feel that these are the best propositions that can be set forth at this time, given the extant literature currently available.

Environment Level

In the literature on organizations, environmental uncertainty and resources have often been viewed as major determinants of organization features, survival, and performance (Aldrich and Mindlin 1978). When the United States suffered from recession in the early 1980s, Lawrence and Dyer (1983) suggested that uncertainty and resources were key considerations in efforts to stimulate the economy. Thus, uncertainty and resources play important roles in economic development.

Studies focusing on uncertainty have tended to measure the complexity and dynamism of environmental conditions (see for example, Duncan 1972), and studies focusing on resources have tended to measure environmental munificence (see for example, Staw and Szwajkowski 1975). Thus, there is considerable precedent in the literature for assessing environmental conditions along those three dimensions—environmental complexity, dynamism, and munificence (Dess and Beard 1984; Sharfman and Dean 1991). Some have noted, however, that environments are multifaceted, and that complexity, dynamism, and munificence do

Exhibit 1
Interrelationships Among Three Levels



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not necessarily correlate across facets. Castrogiovanni (1991), for example, argued that levels of munificence can vary across difference resource pools within a single organization environment. Thus, the research reported here views *environmental* complexity, dynamism, and munificence as broad, guiding concepts, but the propositions indicated in Exhibit 1 focus on the complexity, dynamism, and munificence associated with particular environmental facets important to franchisors, as described below.

Environmental Complexity

Environmental complexity is the range and heterogeneity of environmental elements (Child and Kieser 1981; Randolph and Dess 1984). Since franchising involves the replication of a business format across local markets, it is more likely to succeed when those markets are relatively homogeneous. Julian and Castrogiovanni (1995) found, for example, that U.S. franchisors were more likely to expand into countries with markets similar to those found in the United States than into countries with dissimilar markets (Julian and Castrogiovanni 1995).

Proposition 1a: Franchisors are more likely to enter a developing country to the extent that customer preferences resemble those found in their home countries, all other things being equal.

Furthermore, franchisor costs of entry would be prohibitive unless they could gain economies of scale and scope by establishing multiple units in a given market. Therefore, the market itself should be sufficiently homogeneous to enable business format replication within that market.

Proposition 1b: Franchisors are likely to enter a developing country to the extent that the local market is internally homogeneous, all other things being equal.

Environmental Dynamism

Environmental dynamism is the degree, frequency, and unpredictability of change in environmental elements (Child and Kieser 1981). Many franchisors have difficulty coping with dynamism because they rely on extensive sets of written procedures to ensure consistency across units, and such procedures are difficult to change (Castrogiovanni and Justis 1998). With respect to market entry, franchisors would be especially concerned with dynamic political and monetary conditions because they need assurance that assumptions upon which they predicated their foreign entry and investment decisions will be reasonably accurate (Justis and Judd 1998). Franchisors could suffer huge losses, for example, if they entered a country with a favorable host government only to face a new regime opposed to franchising (or to the particular franchisor's practices) two or three years later. With regard to monetary conditions, franchisors could suffer losses if a foreign market's currency was devalued or experienced extremely volatile exchange rates.

Proposition 2a: Franchisors are more likely to enter developing markets in politically stable countries than in politically dynamic ones, all other things being equal.

Proposition 2b: Franchisors are more likely to enter developing countries with stable currencies than countries with dynamic currency values, all other things being equal.

Environmental Munificence

"Environmental munificence is the scarcity or abundance of critical resources needed by (one or more) firms operating within an environment" (Castrogiovanni 1991). Under conditions of low munificence resources are scarce, and franchisors would find it difficult to survive and generate profit. The particular kinds of resources deemed critical largely depend on the nature of the franchisor's business (Hickson, Lee, Schneck, and Pennings 1971; Rockart 1979). Two key resources critical to all franchisors, however, are monetary—i.e., (1) funds provided by customers in payment for products or services purchased from a franchised unit and (2) funds provided by new franchisees to acquire the franchise and set up operations. In other words, franchisors prefer markets where there is considerable demand for their products or services and an ample number of financially qualified franchisees.

To ensure adequate demand for the products and services of their franchises, franchisors pay particular attention to the population size of their potential foreign markets. All other things being equal, they will tend to enter heavily populated countries like China or India before expanding to their less populated neighbors like Cambodia or Pakistan. By entering heavily populated countries first, franchisors increase the likelihood that sales royalties received from franchises will more than offset the costs of entry (e.g., costs of setting up warehouses, training centers, and other aspects of their franchise support systems).

Proposition 3a: Franchisors tend to prioritize market entry by market size, and so will enter markets with the largest populations first, all other things being equal.

Population density is another key factor associated with market demand (Justis and Judd 1998). Within a given developing country, franchisors will attempt to establish franchises in the major population centers before moving to less densely populated areas, *regardless of the expansion*

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patterns that they previously exhibited in their home countries. Days Inns, for example, initially expanded to various small towns in Georgia exhibiting demographic characteristics (e.g., proximity to interstate highways and vacation travelers) similar to those at their original location. It was later that the company began expanding into large U.S. cities such as Chicago and Miami. When Days Inn entered China, however, the company targeted the city of Beijing, with its population of more than 11 million. By targeting big cities first, franchisors maximize the market demand available to their initial franchise. In many franchised businesses such as fast food, the large, concentrated population of big cities makes it feasible to establish a cluster of units in close proximity to one another, and thereby capitalize on potential economies of scale and scope.

Proposition 3b: When first entering a developing country, franchisors will establish operations in urban areas before branching out to suburban and rural areas, all other things being equal.

The wealth distribution within a market largely determines whether there would be an ample number of potential franchisees. One of the impediments to franchising in Russia, for example, is the fact that very few people have sufficient funds to acquire a franchise (Butrin, Telizina, and Kryukova, 1999). The few who have sufficient funds are mostly Russian entrepreneurs who see no reason to acquire someone else's business concept and format (i.e., to buy a franchise) because they already have their own. Of course, some franchisors may be able to relocate financially qualified franchisees from some other country, as in the McDonald's example described previously, but those franchisees would not have the local market knowledge and related insights that could be beneficial.

Proposition 3c: Franchisors will tend to enter markets where an emerging middle class has considerable investment capital before entering markets where wealth is concentrated among very few individuals, all other things being equal.

Network Level

Whereas the environmental conditions noted above influence franchisor decisions to enter a particular developing country, conditions arising at the network level exert further influences on entry decisions. In addition, network conditions influence the manner in which entry occurs, after the entry decision has been made. Research has shown that franchisors tend to prefer franchising over firm ownership of local units to the extent that three conditions apply: (1) firm resource scarcity, (2) unit monitoring difficulties, and (3) excessive risk (Combs and Castrogiovanni 1994).

Firm Resource Scarcity

Early literature viewed franchising primarily as a strategy for extending distribution channels through geographic expansion (Julian and Castrogiovanni 1995). Theorists argued that access to financial and managerial resources needed for expansion was greater under franchising than firm ownership because franchisees supplied both; thus expansion could take place rapidly (Carney and Gedajlovic 1991). In a study of restaurant chains, for example, Combs and Ketchen (1999) found that available capital varied inversely with the proportion of units franchised. Oxenfeldt and Kelly (1968–69) hypothesized that resource advantages diminish as markets become increasingly exploited because expansion slows to a point where the organization can generate sufficient resources internally. Thus, franchisors would tend to buy back franchises as organizations matured, and franchise organizations eventually would become firm-owned chains. Some subsequent studies, however, found that franchising tends to persist, though a limited amount of buy-back sometimes occurs (Caves and Murphy 1976; Martin 1988; Thomas, O'Hara and Musgrave 1990).

Those studies all provide evidence that franchising is preferable to firm ownership of units (in multiunit chains) when resources are scarce, because franchising eases resource access. In addition, franchises can tap some of the resources (e.g., operating procedures, reputation, etc.) of the franchisor. As noted previously, however, there often are shortages of financially qualified potential franchisees in developing countries. In such cases, franchisors may find it difficult to ease the network's resource scarcities by tapping the resources of new franchisees. Small franchisors are affected most in such situations because they typically have fewer slack resources available for expansion than large franchisors (Oxenfeldt and Kelly 1968–69).

Proposition 4: Large franchisors are more likely to enter developing countries than small franchisors when there are few potential franchisees in the local market that are financially capable of acquiring a franchise.

Unit Monitoring Difficulties

As evidence mounted that resource scarcity alone could not explain why firms franchise, researchers shifted focus to characteristics of the franchisor–franchisee relationship. Theorists argued that geographic expansion makes central control of unit operations difficult and costly (Mathewson and Winter). If the organization cannot bear those costs, it may experience "free-rider" agency problems as unit managers serve self-interests or exert less than maximum effort toward firm interests (Fama and Jensen 1983; Jensen and Meckling 1976). Because franchisees have considerable financial investment at stake and receive unit

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profits, they are likely to be more motivated than managers of firm-owned units; thus, less monitoring is needed.

Norton found that franchised units tend to be larger than firm-owned units, and he argued that this was due to fewer agency problems (1988a, 1988b). Additionally, Krueger (1991) found that wages are higher in firm-owned chains, and he argued that chain-unit managers seem less concerned about maximizing unit profit. Thus, franchising is said to enhance the entrepreneurial capacity of the organization, making unit monitoring less costly than in firm-owned chains. Since monitoring problems increase with geographic distance from firm headquarters (Julian and Castrogiovanni 1995), the difficulties are often considerable when foreign firms expand into developing countries. Consequently, foreign firms would tend to rely more heavily on franchising in developing countries than in their home countries.

Proposition 5a: In developing countries, foreign franchisors will franchise a greater proportion of their units than they franchise in their home countries.

Although franchising can ease some monitoring problems, it appears to bring about a different set of agency concerns. Oxenfeldt and Kelly (1968–69) noted various differences in the sales, profit, and other motives of franchisors and franchisees (Kaufman and Rangan 1990). In fact, conflicts are inherent because franchisors benefit mainly from systemwide sales while franchisees benefit from unit profit (Blair and Kaserman 1982; Inaba 1980; Lee 1984; Zeller, Achabal, and Brown 1980). To increase unit profit, some franchisees gain "free-rider" benefits by shirking on their responsibilities to maintain quality performance—and system sales may suffer from image problems as a result. Also, as entrepreneurs, franchisees often prefer to set their own direction and control their own destinies rather than be controlled by franchisor management (Withane 1991). Thus, franchisees occasionally deviate from franchisor-specified practices because they think they know better ways to do things, even when they are not attempting to free-ride off of the rest of the franchise network. Therefore, while monitoring seems less costly under franchising, it still is not cost free. Franchising creates new agency concerns due to franchisee desires for autonomy and unit profit maximization.

The potential for new agency problems also exists to the extent that environmental complexity cannot be dealt with by the franchisor and therefore is passed along to the franchise level. This situation is more common in professional service businesses than in product distribution or the provision of relatively simple services (i.e., services that most customers could perform themselves but choose to purchase for time-saving and convenience reasons (e.g., maid services). When the business environment is complex, franchisors cannot specify exactly how things should be done, and then they cannot monitor to ensure that things are being done correctly. Dental clinic franchisors, for example, usually do not tell dentists within the clinics how to do their jobs. Thus, considerable discretion exists at the franchise level so that on-the-spot judgments can be made about what should be done in each particular case.

In addition, environmental complexity sometimes makes it difficult to define and measure "good" performance outcomes, and consequently franchisors have difficulties assessing whether correct judgments are being made at the franchise level. If a Century 21 (real estate) franchise fails to sell a listed property, for example, it may be that (1) realtors within the franchise failed to handle the listing properly, (2) seller cooperation in the process was inadequate, or (3) unusual circumstances made it impossible to sell the property. Therefore, to the extent that considerable discretion must be granted to franchisees and their employees, and also to the extent that outcomes cannot be monitored to ensure that such discretion is exercised appropriately, potential agency problems exist. That is, franchisees and their employees may not use their discretion in ways that are consistent with the franchisor's interests. Since these situations are more likely in professional service businesses, franchising is less likely to be employed in that sector.

Proposition 5b: In developing countries, there will be proportionately fewer professional service franchises than product distribution or nonprofessional service franchisors when environmental complexity is high, all other things being equal.

Excessive Risk

Since franchisees typically bear some of the costs of starting their (franchised) operations, franchisors have less investment at risk, and thus have less to lose if a particular franchise is unsuccessful. The possibility of risk sharing, therefore, gives firms incentives to franchise in markets deemed to have excessive risk instead of locating firm-owned units there (Combs and Castrogiovanni 1994). Martin (1988) observed that franchisees face less risk than independent business founders since they tend to experience lower failure rates (Anderson 1984; Castrogiovanni, Justis, and Julian 1993). In exchange for this low-risk route to businessownership, franchisees may be willing to accept relatively high-risk locations. On the other hand, it is also possible that a location deemed risky by a franchisor might be considered less risky by a particular franchisee with detailed knowledge of local market conditions because knowledge mitigates risk. Since developing markets are generally riskier than ones in developed countries, a greater use of franchising would be expected.

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Proposition 6a: The proportion of franchised-to-total units within a network will be greater in developing countries than in developed ones.

As noted previously, franchisors tend to avoid dynamic markets because dynamism brings considerable risk. In some cases, however, they may choose to enter such markets anyway, especially if the market is very large. Then, use of local franchisees would be particularly important because their understanding of local conditions could mitigate some of the risk. Admittedly, the local pool of potential franchisees might be very small in some markets. Because of the risk reduction possibilities, however, franchisors would have considerable incentive to exploit that pool as much as possible.

Proposition 6b: The proportion of local to nonlocal franchisees in a developing country will correlate positively with the level risk that a franchisor perceives to exist in that market.

Individual Level

In their efforts to sell franchises, franchisors often claim that franchised businesses enjoy lower mortality rates than nonfranchised businesses. While that may be true, the evidence is equivocal. Often, franchisors support the claim by noting that only 3 to 4 percent of franchises tend to fail each year while the majority of new business startups fail within their first five years. Such comparison is invalid for two reasons. First, comparison of a one-year rate (for franchises) with a five-year rate (for other businesses) suffers from an inconsistent time horizon. Second, the franchise rate pertains to all franchises, both new and old, whereas the comparison rate pertains to new businesses only percent (Castrogiovanni, Justis and Julian 1993). In a direct comparison of new businesses, Bates found that franchises tended to fail more often than nonfranchised businesses (Bates 1995). In a study of new *franchisor* mortality, Shane found that whole chains tended to fail about as often as the rate attributed to new businesses in general. (Shane did not examine what happens to franchises and their franchisees when franchisors fail, but we might assume that the franchise failure rate is high when the franchisor itself goes out of business.)

These studies, however, have focused on businesses in the United States, and thus the results may not generalize to developing countries. Since the small business sector in the United States is well established, it is relatively easy for new businessowners to develop an adequate support network. Many U.S. business founders, for example, can turn to relatives and friends who own businesses, as well as accountants and other professionals, when problems arise and advice is needed. In developing countries where the small business sector is not well established, there are few such people to which business founders can turn for support. Thus, we might expect the benefits of franchising to be more pronounced in developing countries because franchisors provide a level ongoing support generally unavailable to owners of nonfranchised businesses in those countries. Furthermore, as noted previously, few potential entrepreneurs in developing countries have business training and experience, and franchising can address that limitation because franchisees are given a business concept and training, as well as ongoing support. Through franchising, therefore, potential entrepreneurs in developing countries can attain businessownership without having to "go it alone." Additionally, there is evidence that prior business experience is less important for franchisees than for independent businessowners (Knight). This suggests that the franchising route to businessownership is a more viable alternative than starting a new enterprise, when few individuals have owned businesses in the past. Consequently, new franchises in developing countries are likely to experience greater success than comparable independent venture start-ups.

Proposition 7a: When undertaking new business ventures in developing countries, franchisees will enjoy greater success than independent entrepreneurs in comparable ventures.

In developing countries, the need for entrepreneurial education and management skill development is critical (Telesio 1990). An early study in Hungary revealed that more than half of all Hungarian managers lacked the marketing and financial management skills needed for their firms to be internationally competitive, and significant numbers lacked skills in a variety of other business areas, including organization development and strategic planning. Through faculty and student exchange programs and related endeavors, efforts are being taken to improve classroom business education in developing countries. That, however, is not enough because classroom education in business typically focuses on ideas much more than on skills (Mescon and Vozikis 1979).

For persons seeking to develop business skills, there is no substitute for experience. And through franchising, business skills can be attained and honed. Since business experience and skills are less critical for franchisees than independent businessowners, franchisees can gain skills and experience in a business context where their (initial) lack of skills and experience will not be a handicap. Eventually, some will choose to transfer the experience and skills thus gained to independent business ventures. In those cases, the experience and skills gained through franchising will likely help them to succeed.

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Proposition 7b: Among independent business ventures in developing countries, those started by former franchisees will outperform those started by individuals with no prior businessownership experience.

In sum, franchising can enhance environmental munificence in developing countries by adding to the human resource skill base through the training and experience that franchisees receive. Thus, franchised businesses will likely be more successful than their nonfranchised counterparts (see Proposition 7a), and eventually the knowledge and experience gained through franchising will be diffused to other sectors of the economy as former franchisees embark on new business ventures (see Proposition 7b).

In relatively free markets, businesses providing the most customer value (i.e., customer benefits received relative to the costs incurred) would tend to be the most successful. Therefore, munificence would be further enhanced to the extent that franchising is associated with business success because environmental resources would be used more efficiently. Increased munificence, in turn, would help reduce dynamism because an economic disturbance (e.g., global recession) would have less severe impacts. In addition, increased munificence would make it easier for businesses to access the resources needed to cope with the dynamism and complexity that they face.

Policy Implications

As described above, franchising occupies a middle position between employment and independent businessownership because it offers individuals the possibility of self-employment along with organizational support. In developing countries, individuals accustomed to traditional employment roles can get businessownership training and experience through franchising without having to make the bigger, riskier, and more expensive leap to independent businessownership. By providing such training and experience, franchising can improve the human resource base in developing economies. Since most franchises serve local markets, franchising would increase the competitive intensity within developing countries so that economic resources would be used more efficiently. Then, as business skills gained by franchisees are diffused to other business contexts, nonfranchise enterprises would likely become more competitive in world markets.

In return for providing franchisees with training and business experience, franchisors could profit from current operations. More importantly, they would establish footholds now that could pay off substantially as the developing economies grow. Thus, individuals (i.e., potential franchisees), developing economies, and foreign franchisors investing in developing countries could all benefit from franchising in those parts of the world. To gain the potential benefits, however, franchisors and governments of developing countries must work together. The United States and other countries providing economic assistance can play important roles also.

Exhibit 2 extends the preceding discussions to indicate the role that governments might play. Simply stated, economic development is fostered when business environments exhibit high munificence, low complexity, and low dynamism. To foster economic development, governments can take steps to enhance munificence and reduce both complexity and dynamism. Then, as the economy is strengthened through franchising, conditions will become more favorable for the creation of new independent ventures.

It is axiomatic in the field of finance that the evaluation of capital investments is a function of the expected return and associated risk. Environmental munificence is directly related to expected return because demand and potential revenue are high while resource input costs are low under munificent conditions. This is usually not the case in developing economies, however. For many products or services other than absolute necessities, high demand may not translate into sales revenue because most people do not have much discretionary income. Sometimes, supply channels or the supplies themselves are inadequate, which raises the costs facing franchisors and their franchisees.

Government action is thus needed to enhance the munificence of business environments in developing countries. Munificence might be enhanced, for example, through foreign investment incentives, infrastructure development, site location services, and favorable currency exchanges (Justis and Judd 1998). In addition, voucher systems, credit mechanisms, or other financial arrangements can enable citizens of developing countries to purchase franchises. Since franchising will benefit a developing country more when franchisees are local residents, such incentives should be tailored to encourage the use of local franchisees. For example, governments might give favorable tax treatment to franchisors using local franchisees.

Environmental complexity is closely associated with the cost of conducting business operations. When conditions are complex, they are difficult to understand. Thus costly learning activities are conducted, costly mistakes are often made, and costly monitoring efforts are needed to ensure adequate performance throughout the business system. To a large extent, established franchisors have already dealt with the complexity inherent in their businesses (i.e., in their existing operations). Complexity is enhanced, however, as franchisors expand geographically into foreign countries. Governments might ease this problem by eliminating unnecessary "red tape" facing firms seeking to expand into their countries, and by establishing common standards and other requirements across localities (and perhaps countries) within the region.

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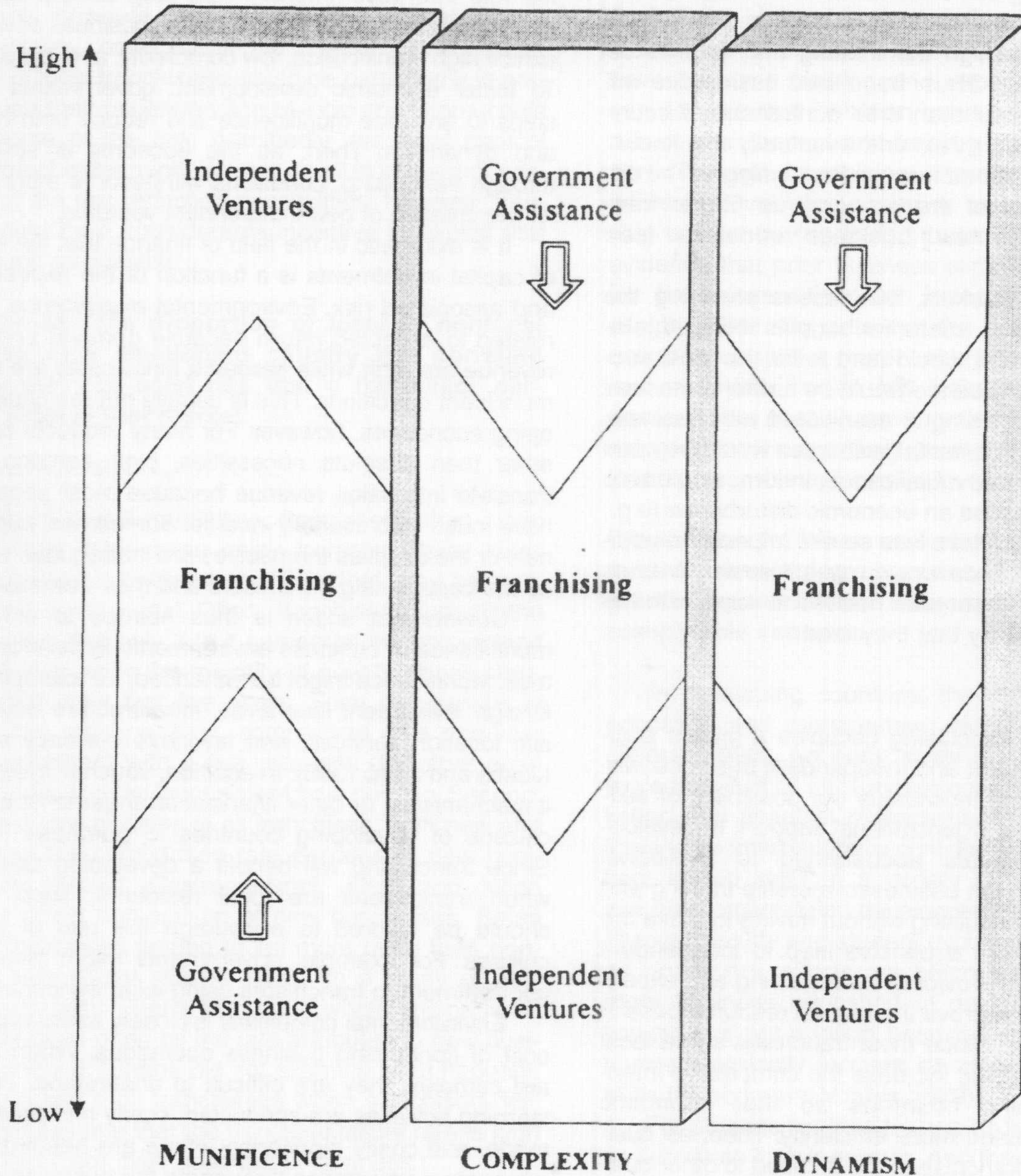

Finally, environmental dynamism is associated with risk. When conditions are dynamic, there is increased risk that actions deemed appropriate in the present situation will prove to be inappropriate over the long run. Since conditions often are very dynamic in developing countries, government action is needed to stabilize the situation. Governments might reduce dynamism, for example, by implementing and enforcing laws (e.g., property rights, trademark protections) designed to protect franchisors and their franchisees (North 1997). In addition, liberal financial transfer policies, possibly including exchange rate guarantees, can eliminate some of the dynamism associated with currency fluctuations.

In return for government assistance, franchisors might agree to certain restrictions designed to ensure that developing countries indeed receive the benefits that franchising can provide. They might agree, for example, to adhere to ethical codes that define franchising and give guiding princi-

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ples as to the obligations of both franchisors and franchisees in such areas as recruitment, advertising, disclosure, franchisee selection, and the franchise agreement. Where none exist, national franchising associations could be formed to help shape policies and agreements between franchisors and governments. By working with such associations, both franchisors and governments could see that their mutual interests are served. Franchisees, in turn, would provide capital, time, and effort to develop successful franchises. Eventually, some franchisees would likely branch out into other entrepreneurial ventures and thus diffuse knowledge gained through franchising to other sectors of the economy.

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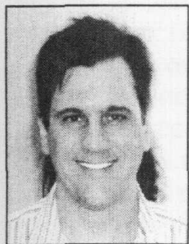

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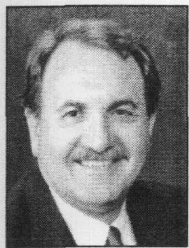

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