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## FRANCHISING AS A MODE OF UKRAINIAN ENTERPRISES' WORK UNDER CONDITIONS OF CRISIS

**Resume** *The relevance of the material stated in article, is caused by influence of crisis on business activity of Ukraine. Objective of this research is to consider franchising as a way of the small and average enterprises effective functioning in Ukraine under conditions of world financial crisis. In the article there is presented the essence of franchising and advantages and disadvantages of this form of business development for both sides of the agreement. The development of franchising is investigated in the world and in Ukraine in 2008-2009. Forecast of the franchising development in 2010 is represented.*

**Keywords:** franchising, franchiser, enterprise, world financial crisis, franchise.

**Аннотация** *Актуальность материала, изложенного в статье, обусловлена влиянием кризиса на предпринимательство Украины. Цель данного исследования – рассмотреть франчайзинг как способ эффективного функционирования малых и средних предприятий в Украине в условиях мирового финансового кризиса. В статье рассматривается сущность франчайзинга, преимущества и недостатки этой форму развития бизнеса для обеих сторон франчайзингового соглашения. Исследуется развитие франчайзинга в 2008-2009 гг. в мире и в Украине. Представляется прогноз развития франчайзинга в 2010 году.*

**Ключевые слова:** франчайзинг, франчайзер, предприятие, мировой финансовый кризис, франшиза.

Nowadays franchising has become one of the most important and vital topics for discussion by professional community. World financial crisis has appeared fatal not only for a small business, but also for the companies – leaders of the market in the sector. Franchising allows large firms to master new market segments and to expand territory of economic activities without attraction of additional capital investments by granting to separate entrepreneurs the right to use an exclusive rights complex of intellectual activity results, goods, works and services that appertain to legal owner. Franchising relations also give considerable advantages for the development of small and average business. Franchisee uses technologies of the legal owner that has stable business reputation with a great demand on production. Franchising also helps to get the advantages in competitive struggle for resources and preferences of consumers.

Validation of considerable economic potential of franchising relations for participants of enterprise activity, in particular, and national economy developments, as a whole, is the wide franchising circulation in foreign countries. "Either franchising, or bankruptcy" is a saying of economists in America. A chance to survive for a firm without franchising reaches only 20 %.

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And it is in the steady market of the West. Today, for example, in the USA the annual volume of retails in franchising sphere reaches more than 40 % of the total amount of sales. It is estimated by the American experts in more than 1 billion of US dollars. Franchising assumes creation of a wide network of the homogeneous enterprises that have the same trade mark. Also entrepreneurs keep up identical conditions, style, methods and forms of goods sales or rendering of services. Standard requirements are the most important for quality of the goods (services) and the single prices established and regulated centrally.

The main franchising advantage is minimization of investments and risks at start of a new business. Chances for success are essentially higher, than those of independent entrepreneurs. Franchisee has an opportunity to use all the advantages of the strong settled brand, common standards of work and servicing, favorable commercial terms, essential marketing support and many other things.

Popularity of franchising consists in effectiveness and high stability of new enterprises. According to "Mr. Doors Home Inc", only 23 % of private enterprises survive after five-year activity in the USA market. Only 18 % of them still exist after 10 years, while only 8 enterprises out of 100 break up in five years, and 10 out of 100 break up in 10 years among those working on franchising system.

Companies with famous brands from the USA, Canada, France, Germany, Japan, Great Britain, and Australia spread their businesses owing to the franchising system. Each eight minutes one franchisee appears in the world because the effectiveness in such companies is twice higher than in ordinary enterprises. Great Britain statistical data testifies that each invested pound of sterling brings six pounds of profit in eight years (whereas the usual enterprise brings only three). German franchising association forecasts stable yearly 10-15 % increase of franchisee objects during the first ten years of the current century. The fact that during the last five years only 8 % of enterprises turned out to be insolvent confirms the economic viability of the franchising system.

One of the main reasons for franchising fast spread and success is the combination of profound knowledge, rich experience and strong financial position of the franchisor — a business organizer, and the franchisee - an energetic businessman, whose enterprise functions as a part of one complex, united by the franchisor.

So a content of franchising is as follows. A franchise is the agreement or license between two legally independent parties which gives a person or group of people (franchisee) the right to market a product or service using the trademark or trade name of another business (franchisor); the franchisee the right to market a product or service using the operating methods of the franchisor; the franchisee the obligation to pay the franchisor fees for these rights; the franchisor the obligation to provide rights and support to franchisees. Franchising is a faster, cheaper form of expansion than adding company-owned stores, because it costs the parent company much less when new stores are owned and operated by a third party. On the flip side, potential for revenue growth is more limited because the parent company will only earn a percentage of the earnings from each new store. 70 different industries use the franchising business model, and according to the International Franchising Association the sector earns more than \$1.5 trillion in revenues each year [1].

Product distribution franchises simply sell the franchisor's products and are supplier-dealer relationships. In product distribution franchising, the franchisor licenses its trademark and logo to the franchisees but typically does not provide them with an entire system for running their business. The industries where you most often find this type of franchising are soft drink distributors, automobile dealers and gas stations. Some familiar product distribution franchises in-

clude Pepsi, Exxon, Ford Motor Company. Although product distribution franchising represents the largest percentage of total retail sales, most franchises available today are business format opportunities. Business format franchises, on the other hand, not only use a franchisor's product, service and trade-mark, but also the complete method to conduct the business itself, such as the marketing plan and operations manuals. Business format franchises are the most common type of franchise.

There are two groups involved in a franchise, the franchisor (the person or company leasing the rights to the business name and system) and the franchisee (the person who purchases it). The right to the franchise is sold by the franchisor to the franchisee for an initial sum of money, often called the up-front entry fee, or franchise fee. This money will be paid once the contract has been signed. The contract (franchise agreement) details the responsibilities of both the franchisor and the franchisee, and is usually for a specific length of time (typically several years). Once the contract expires, it must be renewed. State laws often have an impact on the options for this renewal [2].

This initial franchise fee doesn't include anything except the rights to use the name and system, and sometimes training, procedures, manuals, and other assistance like site selection. It doesn't include any of the necessary inventory, fixtures, furniture or real estate.

In addition to the franchise fee, the franchisee must pay the franchisor royalty fees, or other on-going payments. These payments are usually taken as a percentage of sales, but can also be set up as a fixed amount or on a sliding scale. The terms of these fees will be spelled out in the franchise agreement. These payments are for the on-going services and support that the franchisor provides. Franchisors may also sell supplies directly to their franchisees.

Advertising funds are also paid periodically. These funds are usually put into a general account and used for national and regional promotion for the entire chain.

Franchisee makes the initial installment for the receipt of a licence to use a trademark in the amount of 5-10% of the total cost of creating a single outlet, a periodic fee (usually a percentage of gross income), part of the advertising costs, etc.

According to International Franchising Association, the initial installments for the majority of franchisees are in the range of \$ 20-28 thousand. Periodic fees vary on the average within 3-6% of volume of sales. The average volume of investment needed to create a single outlet, including the cost of real estate is about \$ 320 thousand, but in some cases can exceed \$ 1 million [1].

The franchisor provides personnel development, support in management, an advertising policy and the provision of operational services on demand.

It should be noted that cost of the entrance to the franchise business vary considerably by industry. When it comes to cleaning, filling cartridges and other "non-intelligent" services, the entrance fee is only \$ 5-10 thousand, but the restaurant business amount to \$ 200 thousand. The more popular brand than more possibility of the franchise and above the cost of initial investment, the higher the entry barriers.

USA Today reported that the 10 most popular franchising opportunities are in these industries: fast food, retail, service, automotive, restaurants, maintenance, building and construction, retail—food, business services, lodging.

In addition to franchising, there are two other popular methods by which businesses expand their market and distribution channels: distributorships and licensing.

In a distributorship, the distributor usually has a contractual relationship with the supplier; buys from the supplier in bulk and sells in smaller quantities; is familiar with local markets and customers; may do business with many companies, more than just the supplier/producer; may not receive contractual support and training from the supplier/producer like a franchisee. Some

distribution arrangements are similar to franchises, and vice versa. A franchisee with a great deal of leeway in how to run the business may look like an independent distributor. A distributor may be subject to many controls by the supplier/producer and begin to resemble a franchise.

Some popular distributorships include: Amway, Color Me Beautiful Cosmetics, Mountain Life Spring Water, Knorr Soup Vendor, Campbell's Soup Vending Machines.

Licensing, on the other hand, allows a licensee to pay for the rights to use a particular trademark. Unlike franchises, in which the franchisor exerts significant control over the franchisee's operations, licensors are mainly interested in collecting royalties and supervising the use of the license rather than influencing the operations of the business. Some popular licensors include: Netscape Communications, Apple Computer, Canon Inc., Woolmark, Compaq Computer.

The many advantages and disadvantages of owning a franchise should be carefully evaluated before deciding to purchase one.

Advantages from the Franchisor's point of view:

1. Financial: Franchising creates another source of income for the franchisor, through payment of franchise fees, royalty & levies in addition to the possibility of sourcing private label products to franchisees. This capital injection provides an improved cash flow, a higher return on investment and higher profits. Other financial benefits that the franchisor enjoys are reduced operating, distribution and advertising costs. Of course that also means more allocated funds for research and development. Additionally, there will always be economies of scale with regard to purchasing power.

2. Operational: The franchisor can have a smaller central organization when compared to developing and owning locations themselves. Franchising also means uniformity of procedures, which reflects on consistency, enhanced productivity levels and better quality. Effective quality control is another advantage of the franchise system. The franchisee is usually self motivated since he has invested much time and money in the business, which means working hard to bring in better organizational and monetary results. This also reflects on more satisfied customers and improved sales effectiveness.

3. Strategic: To the franchisor, franchising means the spreading of risks by multiplying the number of locations through other people's investment. That means faster network expansion and a better opportunity to focus on changing market needs, which in its turn means reduced effect from competitors.

4. Administrative: With a smaller central organization, the business maintains a more cost effective labour force, reduction of key staff turnover and more effective recruitment.

Advantages from a Franchisee's point of view:

1. Avoiding the unnecessary trial and error period in starting and operating a new business.
2. Lower financial risk, compared to other ventures, because investment costs are lower and profit margins are higher.

3. Business Format Franchising complete packages ensure a ready to go "turn-key" franchised unit.

4. Managing a small business whilst depending on the power of the franchisor company which has a bigger organization.

5. The franchisee has an opportunity to run a proven business concept with a successful operational track record.

6. The opportunity to learn the latest developments and changes in the local and global market from the franchisor and focus entirely on developing the sales revenues.

7. The benefit of operating under a recognized trade name/trademark, which can have better marketing results.

8. The franchisee has access to accumulated business experience and technical know-how in managing the business.

9. A unified store design which leverages the business reputation in marketing the concept.  
Disadvantages from a Franchisor's point of view:

1. Considerable capital allocation is required to build the franchise infrastructure and pilot operation. At the beginning of the franchise program, the franchisor is required to have the appropriate resources to recruit, train, and support franchisees.

2. At the beginning of the franchise program there is a broader risk that the trade name can be spoiled by misfits until such time the franchisor is capable of selecting the right candidate for the business.

3. There is a risk that franchisees exercise undue pressure over the franchisor in order to implement new policies and procedures.

4. The franchisor has to disclose confidential information to franchisees and this may constitute a risk to the business.

Disadvantages from a Franchisee's point of view:

1. The requirement to pay the franchise fees and royalty to the franchisor, which in some cases can be exaggerated.

2. The transfer of all goodwill built in the local market to the franchisor upon expiration or termination of the franchise contract.

3. The necessity of abiding by the franchisor's operating systems, standards, policies and procedures.

4. Reduced corporate profit margin due to payment of royalties and levies.

For the majority of people, franchising has proven to be the most practicable way to become a business owner. Overall, it offers the lowest risks and the highest level of support. Because a franchisor doesn't succeed until the franchisees do, you'll find a team of dedicated professionals willing and able to help you every step of the way, from site selection to employee hiring to grand opening. They will keep in touch with you from the very beginning to years down the road and have Web sites, toll-free numbers, and an enthusiastic staff to make sure all your questions are answered quickly and completely.

Small and middle business provides 40-70 % of GNP in European countries with highly-developed market economy. The fact that franchising combines advantages of small and middle business adds to its popularity. For most people who are considering business ownership, franchising will provide the least risky means to obtain the financial and lifestyle goals you desire with the best chance of success.

**Table 1** Business Ownership Comparison

	<b>Franchise</b>	<b>Business Opportunity</b>	<b>Your Own Business</b>
Potential Risk Factor	Lower	Moderate	Higher
Cost	Moderate to high	Usually moderate	Whatever you want to spend
Training	Yes	Possibly	None
Proven operating system	Yes	Yes	No
Ongoing support	Yes	No	No
Royalty payments	Yes	No	No
Up-front fee	Yes	Yes	No
Brand-name recognition	Yes	Maybe	No
National marketing fund	Yes	No	No
Marketing help	Yes	Maybe	No
Group buying power	Yes	Maybe	No



Every year Franchise Direct (a member of the IFA) makes a list “The top 100 global franchises” [3]. This study ranks the top 100 global franchise companies from the many thousands of franchises around the world. The ranking is based on objective and measurable criteria including system size based on numbers of units, sales revenue for the system, stability and growth of the system, number of years in operation and market expansion. The ranking is also based on the implementation of best practice in the areas of franchisee support and training, environmental policy and social responsibility.

The franchising industry is an important contributor to the economy of the United States in terms of output and employment. The direct economic contribution of franchised businesses is \$835 billion or around 4 percent of the U.S. private sector economy while over 9.5 million people are employed by franchises. It is also expected for the year 2010 that the franchise sector will produce more than 2 trillion dollars in the U.S. The role of franchising in distributing products to customers worldwide has grown considerably over the past 50 years. The regions most often targeted by US franchises were the Middle East, Western Europe, Central and South America and Eastern Europe.

While franchising is associated with the United States the franchise business model has been adopted globally and there are now major non-US based franchise companies in operation. Nearly 15% of the Franchise Direct Top 100 Global Franchises is comprised of non-US based franchise systems. The ranking includes for example, NaturHouse the Spanish health and nutrition franchise, the Kumon children’s educational franchise which originates in Japan, Cartridge World, the Australian printer cartridge refilling franchise, and Expense Reduction Analysts the UK originated consulting franchise.

In the beginning of the year 2010 Top 10 Global Franchises looked so:

**Table 2** Top 10 Global Franchises

Rank	Name of Franchise	Business Description	Country of Origin	Started as a Franchise Business	Countries	Total Units	International Units
1	McDonalds	QSR	US	1955	117	32,158	13,58
2	Subway	QSR	US	1974	91	32,501	9,432
3	KFC	QSR	US	1952	109	22,2	15
4	Burger King	QSR	US	1954	73	11,5	4
5	7-Eleven	Convenience store	US	1964	15	29,3	22,33
6	InterContinental Hotels	Hotel	UK	1956	100	4,4	1,074
7	Pizza Hut	QSR	US	1959	91	13,1	4,221
8	Snap-on Tools	Home Improvement Store	US	2001	150	3,4	300
9	Taco Bell	QSR	US	1964	100	5,845	245
10	Ramada Worldwide	Hotel	US	1989	47	910	359

Source: 2010 Franchise Business Economic Outlook, prepared by PriceaterHouseCoopers for the IFA.

The Quick Service Restaurant (QSR) industry dominates the Franchise Direct Top 100 Global Franchises. But industry trends look so:

**Table 3** Market Share Distribution by Industry

Franchise Industry	% Market Share	Establishments	% Change over Prior Year
Automotive	4.25%	38,34	1.8%
Commercial and Residential Services	6.33%	57,007	0.3%
Quick Service Restaurants	21.4%	192,827	3.1%
Table/Full Service Restaurants	5.4%	48,609	2.1%
Retail Food	7.85%	70,722	2.4%
Lodging	3.53%	31,827	-0.8%
Real Estate	4.62%	41,63	3.0%
Retail Products and Services	9.8%	88,312	2.3%
Business Services	25.71%	231,151	1.7%
Personal Services	11.11%	100,151	1.8%
Total	100%	901,093	2.0%

Source: 2010 Franchise Business Economic Outlook, prepared by PriceWaterHouseCoopers for the IFA.

Service sector brands focused on everyday needs are one place to start. These include such basics as hair cutting salons, and home maintenance and repair (painting, plumbing, electrical, lawn care, flooring, and handyman services). Automotive service and repair, from oil changes and tune-ups to body work and rim rentals, also tend to stay steady in tough times.

Business services will always be in demand. Franchises offering tax preparation, accounting, computers, legal, and equipment leasing, for example, are evergreens. Some of these services might even be in greater demand as cash-strapped small businesses lay people off and outsource more of their business functions.

As consumers spend less on luxuries and look to save on necessities, dollar stores and used or recycled clothing stores have become more attractive. Rental concepts also are an option for cash-strapped consumers no longer able to purchase expensive items such as high-definition televisions, computers, large appliances, and furniture.

Personal services have remained strong so far, and look to continue. These include child care and supplemental education (art, math, gyms); senior and elder care (home healthcare, nursing, assisted living placement, and legal services); as well as fitness centers for adults (whether a traditional health club or the growing number of concepts providing one-on-one personal trainers).

Reductions in disposable income have been a boon for lower-priced food concepts. Fast-food brands across the nation are offering a growing number of products for less than a dollar. They're also touting value in terms of "bite per buck," adding new menu options, and going the extra mile with customer service. Healthier foods are coming on strong, from probiotic, low-calorie frozen yogurts to trans fat-free fries.

The top global franchises share a number of characteristics which have contributed to their success. These include the following:

1. Strong and internationally recognized brands. The world's leading franchises boast brands that are recognized around the globe and consumers easily associate the brand name and logo with their products and services. For example, with 32,000 units in over 60% of the world's countries, McDonald's Golden Arches and its mascot Ronald McDonald have gained universal recognition. Likewise, with 15,000 units, KFC's Colonel Sander's Mascot is recognized around the world. The 7-Eleven trademarks or International Hotel Group's Holiday Inn and Crowne Plaza also have strong brand recognition.

Brand building within a franchise is assisted by advertising fees which each franchise is obliged to pay the franchisor. These fees provide a constantly growing advertisement fund from

which the franchisor can establish global advertising campaigns. Effective brand management helps the top franchise operations maintain the integrity and consistency of their brands. Wherever the franchise is located worldwide the same quality of product and service is delivered and the same message is communicated.

2. Well defined business model. “In 2010 Franchising will be the most successful way of market expansion.”(J. Naisbitt)

The business model of the Top 100 Franchise companies is well defined and easy to replicate. There is a focus on reliable systems covering every aspect of the operation of the franchise. The business model also has a distinct competitive advantage as it combines strong branding, quality training and entrepreneurial freedom. For example Subway, which is recognized brand around the world, believes strongly in empowering their franchisees. Two slots are kept open on each store's menu board for individual franchisee creations. The simplicity of the Subway business model also means that unlike many of their competitors their restaurant sites are adaptable to any location. There are now over 6,000 Subway restaurants located in non traditional settings i.e. inside Wal-Mart stores, convenience stores, supermarkets, hospitals, schools, military bases and recreational facilities. This strategy has also contributed significantly to the rapid growth of the Subway franchise system.

3. Comprehensive training and ongoing support. The leading franchise companies recognize the importance of intensive training, follow up support and continuous learning. Strong technical and business training ensures customers receive excellent service and quality of products. It also ensures the success of each franchise unit. McDonald's realized from the beginning that the secret to success lies in quality management and competent employees and this can only be achieved through an exceptional training program.

4. Adaptability and Innovation. The most successful franchises are innovative and adaptable to a changing marketplace. The leading quick service restaurant chains for example, constantly offer new choices including healthier options, new toppings, new breads, fillings etc. In 2003, Pizza Hut introduced WingStreet Restaurants due to the rising popularity of chicken wings. Five years later they introduced restaurant quality pastas as people became more health conscious. Also, many of Subway's non-traditional restaurants serve a comprehensive, low-fat breakfast program.

Expansion into international markets can be successful if the target market is researched and a plausible strategy is implemented. A franchise needs to be able to adapt and change to the cultural differences in a new market and to be aware of current trends. For example, in Saudi Arabia, no pork products are served as it is prohibited by Islamic law. All meat sold is halal so McDonalds serves the McArabia which contains no pork products. In Indiana, there are strict religious laws about food preparation. McDonalds have implemented a system where meat and vegetarian meals are prepared in separate areas of the restaurant and chefs preparing vegetarian dishes wear distinctive green aprons to adhere to the local laws. While within Europe, strict EU food regulations made it difficult and expensive for US companies from the food industry to successfully enter the market.

We can also see how the franchise industry can adapt to new trends by introducing new concepts and new ideas for businesses. For example, in response to the ageing of the population there are more franchises set up that provide in-home non-medical companionship and domestic care services for the elderly. Two of these companies have made it into the Top 100 Global Franchises; Home Instead at no. 72 and Homewatch International at position 61.

Nowadays the world is undergoing an unprecedented economic crisis for this generation. Like all businesses, franchisors are watching events unfold, with a feeling that there is little they can do to turn the tide.



Franchisors who have previously been through tough economic times know that the franchising industry has proven itself to be surprisingly counter-cyclical, as more and more laid off employees look to the acquisition of franchises as their next career move. Some are disillusioned with the relative risk of being an employee, while others have a severance package that they end up using to buy a franchise. As many of these people have never owned their own businesses, they are interested in being in business for themselves, but not by themselves, which is what the franchise business opportunity model is meant to offer.

Franchisors pressured by slower unit growth are increasingly looking for innovative ways to help franchise candidates sign on to open new units. Some of these include: reduced franchise fees; lower royalty payments in the startup years; financing assistance; special programs or time-limited offers; help with build-out.

Many economists think that franchising is a better solution to help the country get out of the global crisis quicker than the rest. Franchising, as a business model, fits the qualifications of the affected workers noting that in these times of downsizing and layoffs, many people with management experience are looking for new careers. These displaced workers are the perfect candidates for franchisees that can make a franchise grow. Using the time, resources and network of the franchisee, the franchisor can expand his business. The franchisee, in turn, is given a livelihood.

Franchising is the better business model because it does not require someone to be an entrepreneur in the first place. Being a franchisee is not strictly being an entrepreneur. It is more of being a manager, which is what he was before getting retrenched.

Despite the limited support from government and the financing sectors like banks, franchising has already helped create thousands of businesses and millions of jobs. Capital investments in small businesses create jobs; small businesses have created 60 to 80 percent of new jobs annually over the last decade. Meaningful economic recovery and meaningful job creation will start with small business lending. In fact, the study determined that for every \$1 million in new small business lending, the franchise business sector would create 34 jobs and generate \$3.6 million in economic output.

If we analyze statistics of franchising in the world in 2009, we get the total number of franchise brands. But this data becomes interesting when compared to the following regions/countries of the world (you can see it in the table 4):

**Table 4**

USA+Canada	3000 + 1200
Brazil	1379
Mexico	820
PR China	2600
Japan	1246
Australia	1000
Egypt	340
South Africa	530

After several years of growth in the number of units, jobs and economic output, the franchising industry saw declines in 2009. The specific forecast for that year was: 10,000 franchise units gone; 207,000 jobs lost; \$4.2 billion in the value of goods and services vanishing.

Between 2005 and 2007, the industry found steady growth in all aspects of business, reaching in 2007 some 847,000 franchise units, providing more than 9.8 million jobs and generating \$816 billion in economic output. Growth slowed in 2008 and in 2009 the number of units, jobs

and output all how it was expected to fall, according to the economic outlook report, the first time the IFA has issued such a report.

Some sectors of the franchising industry are getting hit harder than others. Large job declines are predicted in automotive, retail food and retail products and services. Collapsing sales are ripping franchises in the lodging (a 3.2% sales decline), business services (a 2.8% sales decline) and real estate (a 2.1% sales decline) sectors most. Declines in unit growth were widespread across eight different sectors in the study, from business services (2.5% decline) to commercial and residential services (3.5% decline). The only positive notes: quick-service restaurants and table/full-service restaurants were expanded, though not as robustly as before; and sales, too, but that's mainly because of menu price inflation.

But in spite of dark forecast according to a report of the IFA Educational Foundation, franchise businesses reduced employment by 4.1 percent in 2009, resulting in a loss of 409,000 jobs as declining consumer spending caused owners to reduce costs. The number of franchise establishments in 2009 was estimated to have stayed relatively flat, declining 0.1 percent. Output of franchise businesses was estimated to decline by 0.7 percent in 2009, for a loss of \$5.7 billion.

In spite of these losses, franchise business leaders took the necessary steps to keep businesses open and prepare for the economic recovery expected to begin in 2010. The 2009 clearly demonstrated the importance of strong communications and relationships between franchisors and franchisees.

The economic outlook for franchising in 2010 shows some improvement. PwC forecasts that the number of business-format franchise establishments will increase in 2010 by 2.0 percent, from 883,292 to 901,093 — a net gain of nearly 18,000 establishments. After losing over 400,000 jobs in 2009, jobs in franchise businesses are expected to grow 0.4 percent, for a gain of 36,000 jobs. Overall economic output (the gross value of goods and services produced by franchise businesses) is forecast to increase 2.8 percent to \$868.3 billion — an increase of \$23.6 billion — in 2010.

And franchise business leaders are more optimistic about 2010 as well. In a survey conducted by IFA among franchise business leaders, more than half (51.3 percent) of survey respondents say that the economy will be better in 2010, compared to only one-quarter (24.6 percent) of respondents in the November 2008 survey. While more than 78 percent of those surveyed expect moderate to significant increases in franchise units, this is a drop from nearly 86 percent of those surveyed a year earlier.

The survey shows that the issues of greatest concern, both now and in the year ahead, are financing and access to capital. Nearly half of the survey respondents (49.2 percent) ranked “financing and access to capital” as their greatest concern, followed by nearly one-quarter of survey respondents (23.8 percent) who ranked “franchise sales/development” as their greatest concern.

The data show that these concerns are real. FranDATA is predicting a \$3.4 billion lending shortfall in 2010. Banks are expected to lend \$6.7 billion to franchises in 2010, compared to the \$10.1 billion that is needed to meet 100 percent of demand. The shortfall can be attributed to banks' conservative approach to a weak economic outlook and uncertainty in the commercial real estate market. At 100 percent lending, franchise business could create or maintain 305,000 jobs and \$32 billion of annual economic output in 2010.

Also franchising will be the best tool for the development of the small business in Ukraine. For Ukraine, where small and middle business is only in the process of its development, introduction of this type of business is becoming a relevant positive impulse for the economy growth. The franchising development in Ukraine contributes to solving the following problems:

- stimulation of appearance of new competing goods with well-known trademarks, widely advertised in the country and abroad, that will contribute to the expansion of new goods sale markets;
- enlargement of financial and material investments into franchising business on the part of franchisors - residents and non-residents, and also on the part of Ukrainian and Western banks under the guarantee of a franchisor;
- essential enlargement of work places on the labour market;
- further economy development of Ukraine due to the income increase into the country budget.

Franchise agreements in Ukraine are signed from the middle of 90th, however today in the Ukrainian legislation there is not a term "franchising". In jurisprudence there is a term "commercial concession" and legislation is used on the basis of it [4]. However it doesn't hamper the development of franchising and businessmen find the way out from such situation.

Inasmuch as under the franchise agreement the objects of intellectual property rights are granted, the franchise relations shall be regulated not only by the provisions of the Civil Code and the Commercial Code directly governing the franchise agreements, but also by special legislation, namely the laws of Ukraine "On protection of rights to trademarks for goods and services", "On protection of rights to inventions and utility models", "On protection of rights to industrial designs", "On copyright and associated rights".

Ukrainian economists regard the franchising agreement (agreement of commercial concession) to be the most perspective and effective method of business transaction in comparison with all other types of contractual relations, which are based on transmission of exclusive rights on the objects of intellectual property.

Different sources name a number of four hundred franchisers in Ukraine. But for all that, the actually situation is about two hundred of them develop active and constantly. Other are the Russian companies, which want to get into Ukrainian market or Ukrainian companies, which once has opened one or two franchise units.

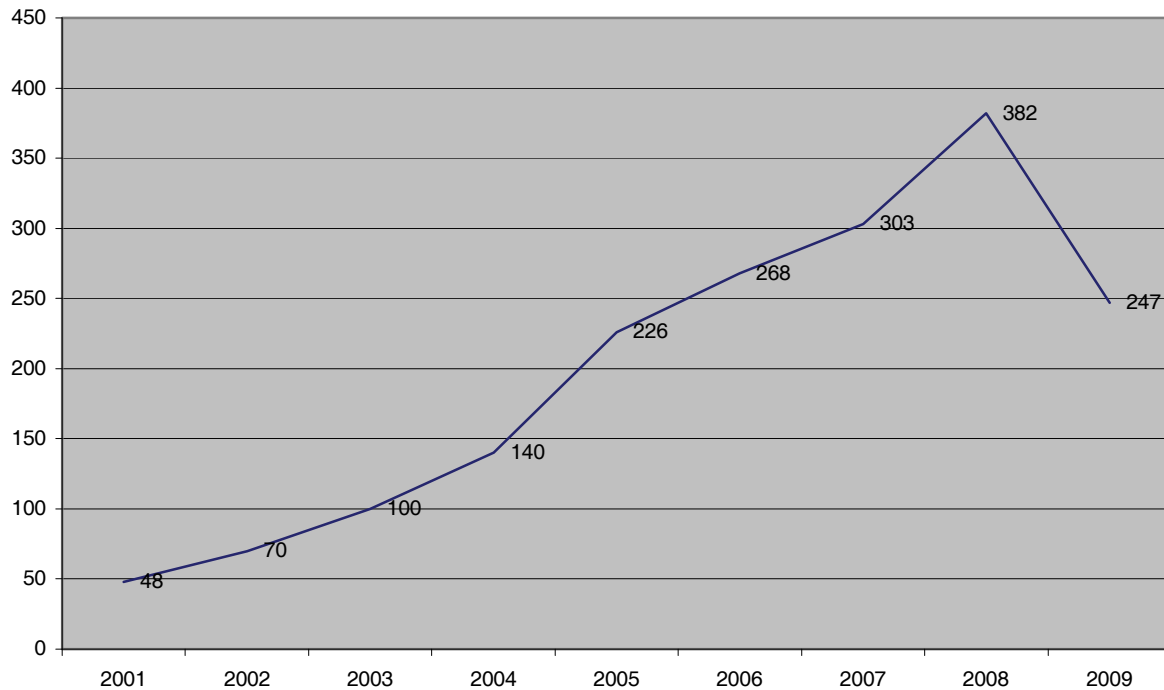
Part of conceptions is adopted from abroad, especially in the field of trade and services. Greater part from foreign conceptions is Russian. Another are from Poland (Atlantic, Cropp Town, Reporter, RuckZuck), Germany (Liqui Moly), USA (International Kids Club, FasTracKids, Crestcom, Sport Life), Italy (Canti Cucine, Colours&Beauty), France (Frederic Moreno, Catimini, Carling), Great Britain (ChipsAway, Hostel) and others. Majority of them – about 60% – opens an own representative office. So, for example, a company Delta Sport develops such known worldwide brands in Ukraine, as Nike and Mexx; MTR-group is engaged in distribution of Broadway, Motor Jeans, Tom Tailor, KENVELO. Other give a preference to collaboration with one partner which gets a right to development of territory of whole country – Helen Doron Early English, FasTracKids and so on.

Every day franchises at the Ukrainian market become more various, new industries and technologies appear. A price range also enlarges: franchisee can choose from cheap franchises of domestic services or rental and expensive franchises of fashionable restaurants and production.

Most Ukrainian franchise systems are concentrated in the capital and only small percent of franchises are by birth from large regional centers. In addition, most of franchise units are situated in the biggest Ukrainian cities - such as Kharkov, Dnepropetrovsk, Donetsk, Odessa and Lviv. But many towns are not yet acquainted with franchising. There is a tendency of glutting the cities and companies redirect in openings of franchise units also in smaller towns.

In terms of the number of Ukrainian companies have claimed positive trend (pic. 1), but given that a number of companies that have suspended their development of franchising, the

key changes have occurred. Really working and most of the essence of franchising - approximately 30 companies. The main reason - a lack of margin development branch network and a network of franchising and its fundamental differences.



**Pic.1** Growth of franchisers' quantity in Ukraine by year

According to the data of Association of Franchising in 2008, number of franchisers increase from 301 to 380 (+26%), growth rate of business made 10 % for the year and numbers of outlets in franchising increase to 33,6 thousand (+85%).

In the first quarter of 2009, some franchisors halted its development program. This primarily affected the companies, where the concept of the business were not good, not worked out the strategy and the process of finding franchisees, as well as promoting their own franchises.

The drop in earnings in the middle and premium segment catering at 30-40%%. The fall in the networks of supermarkets is about 50%, which led many networks to the bankruptcy and the sale of its assets. In the field of construction and building materials - by 60-80%%.

Type of franchising, where the companies used its best efforts so far have remained unchanged, namely: production; trade; service; franchising of business format. Such a conversion, corporate and sub-franchising yet remained unheeded by the Ukrainian franchisors.

Industries are beginning to expand the use of franchising. Thus, if in 2008 they were 12-15 (trade, restaurants, beverages, vending, services), then in 2009 expanded to 20 because there were suggestions of Ukrainian companies in the hotel sector, health and children, design and architecture, distribution, tourism, personnel agencies.

Franchisee (investors) have also increased their activity. For example, if the Triarh Ltd in 2008 received 523 request for the purchase of any franchises, in the first quarter of 2009, already 456 requests, that almost four times higher than the previous year.

Legislative base of franchising in 2008 not been changed by the state, but the ship is beginning to understand the practice of the difference between a contract of «commercial concession» and the «License agreement». This makes Franchisors to draw attention to their contractual basis, and appeal to the experts for the preparation of contracts, as well as the methodology of our work in difficult conditions, lack of registration data contracts.

Attempts to group companies (Triarh, Vasil Kisil & Partners and others) lobby registration commercial concession contracts has been inconclusive. A positive trend is that the round tables and meetings with government officials have the opportunity to bring awareness of the importance of the concept of «franchise» for the Ukrainian economy and enterprise development in the Ukraine.

Many leading world brands have set up offices in the territory of Ukraine to monitor the protection of intellectual property. Personnel for franchising remain the key. If the word «franchise» is not a cause of bewilderment and questions, the essence and standards of franchising are still inaccessible to the majority of managers of companies that declared themselves to the Franchisor.

A crisis amended plans of development of the most franchise systems, majority of franchisees are operating in regions, where now there is rather difficult economic situation. However much, the periodic openings of other franchisors refute stability of this tendency. The most popular franchises in Ukraine nowadays - are those, which need up to \$10.000-15.000, such as: street-food, vending, tourist business and so on.

So after studying of franchising companies' activity in Ukraine it is possible to draw a conclusion that on the one hand 2009 has appeared heavy enough for the development, but on the other hand it has become a kind of a check of concepts on toleration and profitability.

Top-10 of franchising leaders in Ukraine looks like that: «Coca Cola», «Pepsi», «Carlsberg», «InBev», «TNK-BP», «Lukoil», «Empik», "League Invest", «Delta Sports», and also one Ukrainian company-franchisor - «Fast Food System» (FFS). The turnover of leaders is about \$ 850 million per 2009 year. Number of staff who works with franchisor and franchisees - over 200 thousand [5].

In 2009 the total goods turnover has made approximately \$2 billion (4 % of the total goods turnover of the country) in the franchising enterprises working under the license. For example, "TNK-BP" has sold 13 licenses (in 2008 – 17), "Fast Food Systems" has sold 19 licenses (in 2008 – 18) in 2009. So crisis actually has not weakened this segment. Such tendency is observed also in neighbouring Russia and Poland. Crisis was negatively reflected only in two kinds of franchises there: the real estate and "license" luxury in 2009. But inexpensive franchises in a sphere of food, education, trade and services for business have been developing contrary to economic problems.

Franchises in vending (sales of the goods and services through automatic machines) had the greatest demand in Ukraine in 2009. In Association of franchising in Ukraine it was counted that, in this direction, owners of licenses opened 1144 freight outlets, whereas they had not existed in 2008. This year a lot of new franchisors have appeared which have started to develop the networks actively. These are the concepts which do not require big investments (Scorini Caffè Punto, Delice, Enjoy, Kukuruznik, etc.). Also some known big companies declared about their development according to franchising (Insite, Sport Life). Some companies which have started to work in the market in 2008 (The Orange Elephant, Corn House, the Express Manicure, etc.) actively develop their networks. There are also such companies which have closed the franchising projects this year (Ephoto, Linline, Dorozhnaya Karta). The street-food's branch developed very actively in 2009. Franchising networks of the companies which work in this sphere, unite at the moment freight outlets which already number in the hundreds (Fornetti - 600, Chudopech - almost 200, Rumjanochka - is more 100). For trade sphere 2009 has appeared heavy enough: many goods developed networks of foreign brands therefore the dollar rate fluctuation affected their development considerably enough in Ukraine. Therefore it is possible to tell that there was no super considerable quantity of openings in trade sphere in 2009. Some companies



ended up with a brake even point, some opened little franchising shops and some franchisers expanded a network only by opening their own shops. As a whole the companies searched for possibilities of certain concessions for franchisee attraction, they developed anti-recessionary formats and selected assortment. The situation is ambiguous in branch of services for the population. As well as everywhere, concepts with a small amount of investments received the greatest support. For example, a tourist branch was developed very actively, while the expansion of beauty salons and fitness clubs networks was minimal [6].

Franchising is possible to consider as a perspective direction of commercial activity in Ukraine and it is necessary to expect the increase of a number of franchisers and, especially, franchisees. The main reasons of the franchising market growth in Ukraine in 2010 and next years: 1) growth of unemployment of the population (growth of the population interest in its own business creation with application of franchising); 2) economy transition into a recession stage (franchising covers all spheres of economy, some of them will be profitable even under conditions of crisis); 3) a collapse of the share market; 4) a lack of business financing sources (in a case with franchising an entrepreneur diversifies risks and creates steady profitableness); 5) loss in value of real estate and rent (the business basis under franchising conditions creates benefits connected with lower initial capital investments) [5].

The Ukrainian market offers many opportunities for international franchising. However, as an entrepreneurial activity, franchising encounters the same general barriers, as the establishments of small and medium businesses do. These include the whole complex of taxes, high credit rates, crisis of nonpayment, unstable legislation, and very strict control under the subjects of entrepreneur activity by the state. The investment climate remains the major obstacle for franchises in Ukraine.

In order to accelerate the franchising development on the Ukrainian market, regard such steps

should be made:

1) to ratify a law "About franchising", where the rights of franchisor and franchisee would be protected;

2) to enhance activities of consulting and business centers for business plan preparation, management advice;

3) to develop banking crediting and leasing system for franchisee under the guarantee of franchisor (a franchisor could also give a credit to a franchisee on favorable terms);

4) to pay more attention in the institutions, universities, colleges at franchising technology and to investigate franchising experience on real life cases.

Franchising under conditions of crisis will be developing. However, medium-sized franchisers that work without strict system with franchisees can have a number of problems which in the worst variant will be the cause of some companies' liquidation. In the period of economic crisis it is better to trust large franchising networks which take care of their partners.

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