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**Determining the Critical Success Factors of International
Franchising: Cases of Foreign Franchisors in East Asia**

Stephen Choo

INTRODUCTION

Although franchising has experienced phenomenal growth in the United States (U.S.), it has also proven to be highly popular in Europe, parts of Asia, Australia and New Zealand (Chan and Justis, 1990; Preble, 1995). With respect to Asia, Japan was the first country in the region to be targeted by U.S. franchisors in the 1970s (TDB and Arthur Andersen, 1997). As of March 1995, Japan had 158,000 franchised outlets, which ranked the country as the third greatest number of franchised outlets in the world after U.S. and Canada.

Foreign franchisors are attracted to East Asia because it has a soaring middle class, with high disposable income, and more than half of the world's population lives in the region. China alone comprises nearly one-quarter of the world's population and is considered the most under-retailed country in the world (Swartz, 1997). Furthermore, governments in Singapore and Malaysia have recognised franchising as a vital key to stimulate growth in entrepreneurial activities and small businesses (TDB and Arthur Andersen, 1997). The two governments have introduced laws and established organisations and development programs to stimulate franchising in their countries.

There remains a lack of research dealing with East Asia franchising as a high proportion of the investigations into franchising to date have been undertaken in the U.S. This means that much of the franchising literature is based on American experience and therefore may not be necessarily relevant to the environmental background of East Asia. Therefore, this paper has made a significant contribution in determining the factors that are critical to the success of international franchising in relation to foreign franchisors operating in East Asia. I hope that these findings would be studied and utilized by international franchisors looking to expand into the region. The study has identified six categories of key success factors namely distance management, contract enforcement, cultural adaptability, host country risk management, marketing approach and partnership management.

LITERATURE REVIEW

For the purpose of this research, an extensive literature review has been conducted on the capabilities required in international franchising and trends on international franchising in East Asia. Two distinct categories of capabilities needed to franchise internationally have been identified in an extensive literature review (Shane 1996a, Huszagh, Huszagh, and McIntyre 1992; Kedia, et al. 1994). The first category is the level of the administrative efficiency of the international franchise relationship. The second concerns the ability of the international franchisor to operate in a foreign context and directly relates to their level of risk management.

Administrative Efficiency

The level of administrative efficiency inherent in franchising as an internationalisation strategy is concerned with how contractual arrangements facilitate the alignment of preferences between franchisor and franchisee (Brickley and Dark 1987; Carney and Gedajlovic, 1991; Combs and Castrogiovanni, 1994; Lafontaine, 1992). The problem of franchisee evaluation arises when monitoring is difficult or expensive and is exacerbated by a lack of goal congruence and asymmetry of risk preferences between the principal (franchisor) and agent (franchisee) (Jensen and Meckling, 1976). The ability of a franchisor to monitor its foreign franchisees has been empirically identified as an important capability that distinguishes domestic from international franchisors (Shane 1996a). The effects of distance (Heskett, 1986) and culture (Bergen, Dutta and Walker, 1992) combine to further complicate franchisee-agent monitoring, control over service delivery and contract conditions. As a consequence, the ability to manage over distance via systems and the level of cultural adaptability of the franchisor are key international capabilities that need to be developed by successful franchisors.

Distance Management

Many franchise services are location dependent, thus creating a network of service outlets that are physically distant from the franchisor. For the franchisor, the problem of incomplete information regarding their franchisee-agent's behaviour is aggravated by this decentralised service delivery system whose geographical scope extends beyond national boundaries

(Norton, 1988). These problems of geographic distance and franchisee-agent monitoring intensify the problems facing the franchisors' entrepreneurial capability, where both time and distance can raise the level of uncertainty and widen the information gap (Norton, 1988).

Despite technological improvements that may facilitate the transmission of information, it is still difficult and costly to gather and receive complete and timely knowledge about foreign operations. Furthermore, the management of geographic distant locations may involve as much "art" as "science" which is often gained through experience (Aharoni, 1966). The ability of a franchisor to monitor its franchisee-agents over long distances involves a complex set of skills that may not be commonly possessed by the entrepreneurs or managers operating franchise firms and does not necessarily substitute for experience (Huszagh, Huszagh and McIntyre, 1992). These abilities, which include supervisory skills, have been shown to be important for international expansion (Shane, 1996a).

By carefully observing franchisee behaviour, franchisors can control opportunistic behaviour (Norton, 1988). If people are carefully observed, they perceive a greater livelihood of being caught and so reduce their opportunism. Franchisors can monitor against opportunism by inspecting franchisee facilities, examining their records, and by specifying and verifying equipment usage or minimum standards. Therefore, monitoring is a capability that franchisors develop.

A second important aspect of distance management is the structure of the international franchising contract, which is a central aspect of the franchisor-franchisee relationship (Rubin, 1978; Lafontaine and Kaufmann, 1994). Within the franchisor's domestic market, most contracts between the franchisor and franchisee are standardised (LaFontaine and Kaufmann, 1994), thus simplifying general contract management. Contract details such as fees, royalties, advertising contributions and length of agreement vary little from franchisee to franchisee within the domestic context. However, within the international market, franchising contracts can vary substantially (Abell, 1990).

According to Shane (1996a), international franchisors may need to modify contracts to include the initial terms of their franchise agreements, the ratio of their franchise fees, and provisions concerning cooperative advertising and store opening support. Such variations with an international contract may be due to the size of a franchisee, host country restrictions, local business practices, and the opportunistic behaviour of particular franchisees. It is important that franchisors have the ability to negotiate contract modifications (Root, 1987) and handle contract enforcement in order to achieve successful international development (Hood and Young, 1979).

Cultural Adaptability

The differing cultural environments found in foreign markets add further complexity to international franchising (Huszagh, Huszagh, and McIntyre, 1992). A cultural environment that is significantly different from the franchisor's home country may affect not only the contract negotiation process (Weiss, 1996), but also issues such as recruitment and selection of personnel, and the franchise format (Justis and Judd, 1989). The very strength of the franchise format, its standardisation, makes its successful replication in foreign markets difficult (Aydin and Kacker, 1990). Frequently, modifications may be needed. This may not just involve recipes and menu selections, but in the operations as well (Sadi, 1994). Embedded in the operational routines and processes are assumptions about how work should be done. Variations in cultural norms such as "power distance," Confucian dynamism, and individualism can affect local implementation (Hofstede, 1980).

Host Country Risk Management

The second set of capabilities to succeed in international franchising involves the ability to deal with uncertainty within the overseas host country. Risk management is an important consideration in international business research (Ghoshal, 1987). Issues such as government policies, regulations and macroeconomic variations make conducting business internationally more uncertain than domestically (Miller, 1992). Hackett (1976) indicated that such issues were important to franchisors. The franchisors in his survey were primarily concerned with government regulations within the foreign market that affect both the conduct

of the service and monetary uncertainty, rather than the complexities of format modification. Therefore, host country policy evaluation and foreign exchange management are fundamental capabilities that are important for international franchisors to develop.

Host country policy evaluations. The primary problems that international franchisors encounter in relation to foreign government policy are restrictions on the ownership and control of corporate assets and intellectual property, as well as repatriation of profits, interest, royalties, and principal repayments (Aydin and Kacker, 1990; Lafili and Van Crombrughe, 1990). It is important that international franchisors have the ability to evaluate these aspects of foreign government policy. Unfortunately, this set of management skills may be the hardest to develop because of the complexity of foreign regulations and the time and resources required to develop such expertise. Advice on such issues is available from many franchise consultants and small business agencies, but may be too expensive for some smaller franchisors (Fladmoe-Lindquist, 1996).

As many franchise businesses have a service-base, it may be easy for competitors to imitate the firm's business model. As such the protection of intellectual property becomes a fundamental concern for many franchisors (Lafili and Van Crombrughe, 1990). Franchisors need the ability to monitor the franchisees' use of their brand name and trademarks, including the specific details of management systems, designs, or processes that constitute core elements of the system (Justis and Judd, 1989). However, the protection of brand name, trademarks and reputation is not easily managed in countries where intellectual property laws vary or are not enforced.

Exchange risk management. The need to manage the effects of exchange rate movements arises from the impact of fluctuating home and host country exchange rates on franchise contracts (Huszagh, Huszagh, and McIntyre, 1992). Large and frequent swings in foreign exchange rates demand particular capabilities and expertise. For example, many franchisors require that some inputs into the franchise operation be imported from the home country. Therefore, any major change in the exchange rate can increase the franchisor's economic exposure as well as impacting negatively on the market. Many of the potential problems of fluctuating exchange rates may be proactively managed by the use of periodic rate adjustment and payment terms expressed in percentages (Meroni, 1990). However, this requires specialist skills not commonly found in most domestic franchisors.

INTERNATIONAL FRANCHISING IN EAST ASIA

By the end of the 1990s, the ubiquitous presence of U.S. fast food chains in East Asia stood as testimony to the success of international franchising in this region. When Western (predominantly U.S.-based) fast food chains first entered East Asian markets, many sceptics argued that Asians would never develop a taste for hamburgers and pizzas, and that their presence would only be a passing fad (Wee, 1997). Such arguments were not unfounded. The prices of these Western fast foods were not cheaper than local fast food. Further, it would have been plausible to believe that Asians, who had grown up on rice and vegetables, would never fall for "junk" foods.

Despite these misgivings, the Western fast food outlets like those of McDonald's, Burger King, Kentucky Fried Chicken (KFC) and Pizza Hut became familiar sights in any major city such as Singapore, Hong Kong, Manila, and Kuala Lumpur. Average sales per store in Asia for KFC are US\$1.2 million, compared with US\$750,000 in the U.S. The difference occurs even though most Asian markets have much lower per capita income than the U.S. (Tanzer, 1993). Hong Kong, with a population of around six million, was home to five of the world's 10 busiest McDonald's (Love, 1995).

Strong marketing positioning by the western fast food franchisors was identified as one of the key factors for their success (Love, 1995; Watson, 1997; Wee, 1997). In East Asia, there is a plethora of cheap and tasty foods that are easily available. It was unproductive for western fast food chains to compete head-on against these local operators on the basis of food. Instead, these franchisors have positioned themselves as a lifestyle phenomenon by offering other benefits such as courteous service, air-conditioned comfort, hygienic and efficient food

preparation, clean toilets, brightly lit dining areas, modern and attractive ambience, and constant but varied promotional offers.

According to Chan and Justis (1992), the proliferation of franchising in East Asia is due to several economic and demographic trends. Some of them include universal cultural trends, increased disposable income, increasing number of women in the workforce and demographic concentrations of people in urban areas.

Two western franchises that have proved particularly successful in East Asia are Pizza Hut in Hong Kong and KFC in Malaysia. Pizza Hut Hong Kong is owned by Jardine Pacific and a Marketing Management winner of the Asian Management Awards. Jardine Pacific is a leader in the Asia-Pacific region, with approximately 300 outlets and more than 8,500 employees. These operations include the world's largest international franchisee of Pizza Hut, as well as Taco Bell, Ruby Tuesday, and the "Nine to five" restaurants, plus the Oliver's Super Sandwiches chain.

In Malaysia, KFC is owned by KFC Holdings (Malaysia) Berhad, which is a publicly-listed company on the Kuala Lumpur Stock Exchange. The company operates restaurants, a convenience food store chain, a poultry processing and poultry retail chain, breeder farms, hatchery, broiler farms and a feedmill. KFC Holdings' sales were reported as US\$153 million in 1999 and the company owned 289 KFC stores (for more details visit <http://www.kfcholdings.com.my>). Effective marketing, vertical integration and strong, stable management were reportedly responsible to its astounding leadership position of 60 per cent share of Malaysia's fast food market (Astbury, 1992).

Although U.S. franchisors are perhaps among the best known, many Asian franchises have entered the sector and learnt to compete with and even beat their famous Western counterparts in their own game (Prystay and Kumar, 1997). One such company is Jollibee, a Philippine hamburger chain. With 302 outlets it is the clear market leader, making the Philippines one of only two countries in the world where McDonald's is not the market leader. Much of Jollibee's success at home and abroad is tied to the greater variety of foods found on its menu and the taste that is more suited to Filipinos.

RESEARCH METHODOLOGY

This research is designed as a multiple-case study comprising four purposely-selected foreign franchisors that have expanded into East Asia. A case study is considered a more appropriate strategy for answering research questions which ask 'how' and 'why' and which do not require control over the events (Yin, 1994). This is because such questions deal with operational links that would need to be traced over time, rather than mere frequencies or incidence. By using the case study approach, the reasons why certain decisions were made, how they were implemented and what the results are can be identified. The research into international franchising has been largely quantitative, which makes its complexities very difficult to be tracked and studied in detail. The decision of carrying out case studies was that they are valuable as preliminaries to major investigations as they generate rich data that may suggest themes for more intensive investigation (Burns, 1990).

Eisenhardt (1989) states that in the multiple-case approach there is no ideal number of cases, but suggests that a study of between four and 10 cases usually works well. With fewer than four cases, theory is difficult to generate, and with more than 10 cases, the volume of data is difficult to cope with. For this study, four foreign firms that have had several years of experience operating in East Asia were carefully selected. In particular, a failure was intentionally picked because it provided a "control set" which provided a meaningful contrast to the other three firms, which were experiencing success in the region.

In this study data were collected primarily via two methods: in-depth interviewing and documents research. In-depth interviewing (face-to-face) was a data collection method relied on quite extensively in this study. The interviews were conducted with key decision makers involved in the internationalization of the firms. They included managing directors, founder, international franchise managers and overseas master franchisees. All the interviews were

tape-recorded and then transcribed. The typical interview lasted two hours; the length varied from 90 minutes to three hours.

A guideline for interview questions was provided in Appendix A. It consisted of 22 open-ended questions. Each question, however, was only a point of reference. During the interviews, questions were neither repeated verbatim nor in a given order. The importance of this guideline was that it provided some directions for the interviews. Typically, the researcher began the interviews with questions similar to the questions suggested in the guideline, and then depending upon the responses received, he moved into probing questions. Probing questions were useful in gaining more insights and clarifying the answers from the respondents.

The researcher explored a few general topics regarding international franchising to help to uncover the respondents' meanings and perspectives, but otherwise respected how the respondent framed and structured the responses. This was to ensure that each respondent's perspective on issues of international franchising became unfolded as the respondent viewed it, not as the researcher viewed it.

In keeping with the case study method, document research or multiple sources of data collection were used to provide triangulation. Documents are good sources of evidence, because many documents are easily accessible, free and contain information that otherwise would take an investigator substantial time and resources to gather (Dexter, 1970). The data were collected from documents such as annual reports, minutes of meetings, letters, internal memoranda, court proceedings, newspaper clippings, magazine articles and books.

Data analysis is the process of bringing order, structure and meaning to the collected data. Merriam (1988) and Marshall and Rossman (1989) contend that data collection and data analysis must be a simultaneous process in a qualitative research design. The method of qualitative analysis here draws on Yin (1994, p. 103)'s preferred strategy of relying on theoretical propositions that led to the case study. The propositions helped to organize the case study and to examine alternative explanations.

Both single case and cross-case analyses were included in this study, and the process of data analysis entailed three activities: data reduction, data display, and conclusion drawing and verification (Miles and Huberman, 1994, pp. 10-3). These activities proceeded concurrently during the research project, although one might take precedence over the others at various times.

Data reduction refers to the process of selection, focusing, simplifying, abstracting, and transforming the data that appear in written-up field notes or transcriptions (Miles and Huberman, 1994). The process of data reduction in this study began as soon as the important topics or themes were identified and continued throughout data collection and report writing.

The writings of Miles and Huberman (1994) were drawn on for techniques of data display. They suggest that data displays should be designed to assemble organized information in a compact form that is immediately accessible. One of their techniques, which was used in this study, was to arrange empirical evidence in tables in the forms of words, rather than numbers. By looking at these tables, themes that agree or disagree across cases would emerge.

Drawing conclusions and verifying them took place before, during and after data collection. Before data collection the researcher might have had vague and unformed hunches that could lead to conclusions. As analysis proceeded, however, these conclusions were tested and elaborated systematically for their soundness, the conclusions then became more explicit as they were verified by the data in increasingly grounded analyses.

The primary strategies that were utilised in this study to ensure validity included (a) providing the provision of rich, thick, and detailed description so that anyone interested in transferability will have a base of information appropriate for comparison (Lincoln and Guba, 1985) and (b) by conducting a cross-case analysis.

To ensure reliability, three strategies were employed in this study: (a) the researcher provided a detailed account of the focus of the study, the researchers' role, the participant's position and basis for selection (Goetz and LeCompte, 1984); (b) multiple methods of data collection and analysis were to strengthen reliability as well as internal validity (Merriam, 1988); and (c) data collection and analysis process were reported in detail in order to provide a clear and accurate picture of the methods used in this study (Merriam, 1988).

Data reduction, data display, and drawing conclusions were activities of data analysis occurring interactively throughout the study. All the three activities were, therefore, combined to produce a comprehensive analysis of the study.

SUMMARY OF CASES

For this study, it was decided that the multiple-case approach (see Eisenhardt (1989) and Yin (1994) for more details) was more appropriate to ask the 'how' and 'why' questions. Each of the cases was selected for this study because it either predicts similar results (literal replication) or different results for expected reasons (theoretical replication) (Yin, 1994). The franchise firms chosen for this study were Dome Coffees (Australia), The Body Shop (U.K.), Royal Copenhagen Ice Cream (Australia), and Coffee Bean and Tea Leaf (U.S.). A brief summary of each of the cases is presented to provide a background to enhance the interpretation of the research findings.

Dome Coffees is a retailer of coffees in Australia, Southeast Asia and the Middle East. The company operates 48, mostly franchise, outlets around Australia, Malaysia, Singapore, The Philippines, Indonesia and the United Arab Emirates. The company also has a coffee roasting business based in Australia, which roasts coffee from 16 different countries and sells to the Dome cafes and other outlets. Each week, it airfreights hundreds of kilograms of coffee to The Philippines and United Arab Emirates, with its Singapore factory roasting coffee for cafes in Singapore and Malaysia. Over the past 10 years, the company has grown from a single café to an international AUD\$60 million-dollar international enterprise (for more company details visit <http://www.Domecoffees.com.au>).

The Body Shop is a value-driven, high quality skin and hair care retailer operating in 49 countries with 1,730 outlets spanning 25 languages and 12 time zones in 2000 (Annual Report and Accounts, 2000). The company is famous for creating a niche market sector for naturally inspired skin and hair care products. It is estimated that in 1998/99 the Body Shop sold a product every 0.4 seconds with over 84 million customers transactions through stores worldwide, with customers sampling the current range of over 600 products and more than 400 accessories. The success of the Body Shop, both in the U.K. and overseas, has been well documented and the growth of this company that eschews advertising and puts principles above profit, has left many a hard-nosed business executives bemused (*The Body Shop: Timely Arrival in Hong Kong*, 1991). In the company's 1998 annual report, The Financial Times voted The Body Shop the 27th most respected company in the world (for more company details visit <http://www.thebodyshop.com>).

Coffee Bean and Tea Leaf (CBTL) was started in 1963 and it remains one of the oldest gourmet coffee stores in the U.S. In July 1999, the original founding family sold a substantial share of CBTL to its master franchisee, the Sassoon family, in Singapore. Currently, this privately owned family business is based in Los Angeles (LA). CBTL's coffee roasting plant still remains in LA, which vacuum packs and distribute its coffee worldwide. The firm's proprietary ice-blended mix, which is considered to be a company's trade secret, is shipped to all its overseas operations. Since the acquisition, the business has aggressively grown the number of outlets to 192 worldwide over the past 36 months (for more company details visit <http://www.coffeebean.com>).

Royal Copenhagen Ice-Cream (RCIC), started in 1983, operates premium ice cream stores in both street front and shopping centre locations throughout Australia. Each shop produces its own ice cream and bakes its own fresh cones daily in front of customers. Décor is Danish with warm colours, and staffs wear Danish looking uniforms. RCIC's entry into international market began in 1991 when it expanded into Singapore. Since then, it had sold franchises to

Thailand, Indonesia, Malaysia, Japan and the Philippines. From 1991 to 1997, the company had 23 stores in Singapore (3), Thailand (11), Malaysia (3), the Philippines (2), Indonesia (3) and Japan (1). However, the 1997 Asian economic crisis had a severe impact on all its overseas franchises, which led to the complete withdrawal of the brand from all of its Asian markets.

RESEARCH FINDINGS

The method of qualitative analysis employed in this study draws heavily on the techniques of Yin (1994) and Miles and Huberman (1994). In addition, a coding analysis (reducing the data to key events in key categories) was undertaken which found six main categories namely distance management, contract enforcement, cultural adaptability, host country risk management, marketing approach and partnership management.

Distance Management

Strong capability in distance management, which includes the constructs of control and monitoring, field support, key staff management, information exchange, and franchisee training, was found to enhance success in international franchising in East Asia. This ability also serves as an effective mechanism for controlling franchisee opportunism (Norton, 1988).

While it has been acknowledged that monitoring franchisees closely is effective for controlling franchisee opportunism, the means by which it is carried out is a delicate issue within franchising. Too much control might be counter-productive (Stanworth, 1995). The desire for independence, autonomy and self-fulfillment remains a basic motive for franchisees to join the franchise systems (Peterson and Dant, 1990). Hence, excessive levels of control might not be welcomed and may even impact adversely on franchisees' performance levels. The study found a high variation in the control and monitoring of master franchisees exercised by the firms. Dome, The Body Shop and CBTL closely control and monitor their master franchisees' foreign operations to ensure consistent quality while RCIC practiced a *laissez-faire* approach in their managing of franchisees.

For example, Dome conducted regular audits to monitor the progress and performance of the franchise operations in all its overseas markets. The audits are conducted quarterly during the first year, bi-annually during the second year and annually for subsequent years. Each outlet is being audited comprehensively on 132 items. In contrast, there was little mention of control and monitoring by RCIC of their previous foreign franchisees in Asia.

In franchising, monitoring frequently requires the direct observation of the activities of franchisees. The effect of distance intensifies the ability of the franchisor to closely monitor the foreign franchisees' activities. There is a need for international franchisors to have adequate human resources who have supervisory capability to undertake this observation (Combs and Castrogiovanni, 1994).

The study found that close control and monitoring is closely associated with the franchisor's level of field support. All firms, except RCIC, have regional offices in Singapore to provide pre-opening, administrative and marketing support to the markets in the Asian region. In the case of Dome and CBTL, managers are regularly sent from the head or regional office to visit the outlets either for training or auditing.

In the early days of Dome's operation in Singapore, the franchisor spent considerable time working with the local key managers to 'fine-tune' the business format. This suggests that the franchisor should be running a successful domestic operation, with strong administrative and management support, that allows him or her to spend considerable time away from the business. Shane (1996a) pointed out that the higher the growth of the franchisor, the more successful it is, and therefore the more resources it may have to devote to its globalization efforts. This is likely to be a challenge for small firms that lack adequate managerial resources to permit time for such intensive commitments to offshore franchise developments.

Sachdev, Bello and Pilling (1994) referred to the provision of information by the franchisor to the franchisees as a device for influencing franchisee behaviour. This is seen as an indirect

form of control. Dant, Li and Wortzel (1995) have also found that information exchange can contribute significantly to improving the quality of franchisor-franchisee relationship.

When asked about information exchange between franchisor and franchisees, Dome's regional general manager (RGM) said: "Communications between the franchisor and the foreign master franchisees are at most times confined to the top management only." In some instances this results in a breakdown in communication as the message filters from top management to the frontline staff. To prevent such an occurrence, the Dome's RGM ensures that every staff member at all the foreign outlets knows him personally. As the level of knowledge amongst the operational staff is relatively low in these markets, he frequently receives a telephone call from an outlet manager or a cook when a problem arises. This evidence on regular communication is also found with the Body Shop. The firm's head of franchising believes that managing franchisees in Asia is "all about relationship." He further adds, "in Asia they don't really tell you what they are thinking as they are not confrontational, therefore you have to spend a lot of time with them to find out what it is."

Dependency of the franchisee on the franchisor for training has been identified as one of the mechanisms available to the franchisor to ensure compliance and so mitigate against dilution of goodwill (Burton, Cross and Rhodes, 2000). The study found that the initial pre-store training of the master franchisees for the firms was conducted in the home country. For example, the Singaporean master franchisee and key managers of CBTL spent six weeks training in the U.S. Dome's key managers were trained in Singapore for a month. However, the difference between the RCIC and the rest was the level of continuous training provided to the master franchisees.

For example, Dome in Malaysia has a full-time local training manager, who works very closely with the franchisor's regional general manager, dedicated to managing the continuous training needs of all the staff. In contrast, RCIC visited its master franchisees only once or twice a year to provide continuous training.

Contract Enforcement

Overall all the firms, with the exception of The Body Shop, appeared to be making few modifications to their international franchise agreement, which was the template used for domestic franchising. These firms relied heavily on the professional expertise and advice of their solicitors who specialise in domestic and international franchising. Therefore, having an appropriate solicitor who specializes in international franchising will compensate for the lack of ability to negotiate contractual modifications and handle contract enforcement.

The negotiating power of a franchisor has been found to be largely dependent on the degree of success the franchise brand enjoys in the region. Dome's schedule of fees for its Indonesian master franchisee is considerably different to its previous master franchisees. The firm was able to insist on a higher franchise fee, from US\$75,000 to US\$100,000, because of its successful track record in Asia. Therefore, it will be extremely difficult for a foreign franchise firm, which expands into East Asia for the first time, to impose a high upfront franchise fee to reduce franchise opportunism.

This should be worrying for any potential foreign franchisor, especially when it is found that most East Asian master franchisees have a tendency to highjack the franchise brand. When they get bolder, they will likely to 'hijack' the brand. Why do Asian franchisees exhibit such 'brand hijack' behaviour? This could be attributed to three reasons. The first could relate to the ineffectiveness of the initial franchise fee or ex-ante bond. The second could be due to the unsophisticated level of legislative protection of intellectual property rights found in most parts of Asia. Finally, the franchise concept in Asia could differ greatly to the franchisor's original business format in the home country. This is perhaps due to the modifications that the master franchisees forced upon the franchisors to make to adapt to Asian consumers.

According to Combs and Castrogiovanni (1994), the bond serves as a particular effective tool when the franchisee invests a large percentage of his or her money in the purchase of the outlets. Under these circumstances, termination of the franchise agreement often results in great financial hardship for the franchisee. The preference shown by most master

franchisees in Asia to own all their stores within their territories requires the franchisor to work with a company rather than an individual. The franchise fee would have to be a significant amount, in order to be operative as an effective tool to prevent a company from acting opportunistically.

Cultural Adaptability

Cultural adaptability was found to influence the performance of international franchisor in East Asia. This indicates that the franchisor should not only adapt the product, price and business format but the way franchisee relationship is traditionally being managed in the domestic market if success is to be had in East Asia.

The debate over standardisation versus adaptation is an ongoing one within the international marketing and internationalisation literature. Franchising requires a high degree of standardisation to be effective, however, in foreign markets the pressure to adapt the product or service is frequently great. The local partner (with local knowledge) is frequently the party with the greatest ability to find suitable adaptable strategies. This may result in the power of the relationship shifting towards the master franchisee in countries where the level of adaptation is greatest.

The study also found that franchisors practice both standardisation and adaptation in their international operations in East Asia. This practice emanates from the concern of the franchisors in losing the integrity of the franchise concept, which is found in the standardisation of the business format, if too many alterations to the franchise's core product or service are being made. Standardisation is found in the franchise brand image and value while adaptation, albeit allowed on some of its products or services, is being closely monitored by franchisors.

Dome's case illustrates the practice of brand standardisation. In Australia, Dome's brand image is one of style and sophistication, which is reflected in its store design, products, ambience and packaging. The early cafes in Asia resembled the Australian cafes in every detail, from the design and interiors right down to the chairs. Dome's RGM explained: "Our branding, image and marketing principles must be strictly adhered to by all our franchisees...we may lose some customers but they will come back as they associate us with the good things in life. It is a place to see and be seen."

Adaptation has also been applied to the product offering by all the firms, with the exception of The Body Shop. In their home countries these firms have a limited range of food items in their outlets. However, they had to include a wider range of hot food items in Asia as Asians need to have food with their coffees and the high rental costs would make it nearly impossible to survive just by selling coffee alone. In contrast, the Body Shop makes no modifications to all its products sold worldwide. The only thing that is different is the retail-mix. For example, skin care products are more popular in Asia, where it is mostly hot and humid, than bath products. Unlike food which is culturally sensitive, hair and skin-care products can be considered a 'global product' that requires no modification to suit cultural differences.

In the case of Dome, master franchisees are not allowed full autonomy in modifying the menu to suit local tastes. However, the company keeps a close watch on any new product innovations that are being introduced by the franchisees. This is critical to maintain the integrity of Dome's concept as foreign master franchisees are often tempted to introduce local fare to satisfy its customers. The solution is to 'domify' the local food by giving it a Dome appearance, which gives it a fusion theme to maintain the European presence.

Host Country Risk Management

This study did not find any strong capability in host country risk management possessed by all the firms, with the exception of The Body Shop. The complexity of foreign regulations can be difficult for a smaller franchise firm to grasp, as it requires a considerable amount of time and money to develop such a capability. This research indicates that the smaller firms rely heavily on their local master franchisees in the target market. This behaviour results in smaller franchise firms preferring unsolicited enquiries when entering into culturally distant markets such as East Asia.

All of the cases prefer unsolicited enquires to enter into new markets. They believe that when a potential franchisee has taken the initiative in making the first approach, he or she would be aware of the magnitude of risk entering the chosen foreign marketplace. It was felt that such a franchisee would be more likely to take up the franchise because "he would have already liked the concept," than someone just simply replying to an advertisement in the press. The franchisor also relies on potential master franchisees' knowledge and information on foreign market risk. The joint managing director of CBTL said: "We never go to them, they came to us as it is the most effective means of recruiting potential master franchisees, we're not like the large franchise firms. We're small so we don't have any resources to undertake international marketing." Therefore, it is important for a smaller franchise firm to work with a master franchisee in East Asia who has the capability to evaluate foreign country government policies.

The need to manage the effects of exchange rate movement arises from the impact of fluctuating home and host country exchange rates on franchise contracts (Huszagh, Huszagh, and McIntyre, 1992). Many franchisors require that some inputs into the franchise operation be imported from the home country. Therefore, any major change in the exchange rate can increase the franchisor's economic exposure. There was no evidence of franchisors, with the exception of the Body Shop, possessing this particular capability in managing exchange rate movements. This could be attributed to the complexities in managing exchange rates that fluctuate on a daily basis. Dome negotiated and agreed with all the master franchisees on a fixed U.S. dollar exchange rate for between three to six months. Meroni (1990) has also found this periodic rate adjustment approach being used by international franchisors.

Dome's international director explained: "You can have a sophisticated system of managing exchange risk, but fixing a rate for a certain period is uncomplicated to administer and understand." In contrast, the Body Shop has a very sophisticated exchange risk management system that involves the use of forward foreign currency contracts.

Marketing Approach

The study reveals that a unique form of master franchising is practiced in East Asia. Instead of sub-franchising the units, the master franchisees prefer to own and run the entire units. When the CEO of CBTL was asked why, he said: "The reason is attributed largely to the limited size of the marketplace as the products are targeted at specific niche markets rather than the general public...coupled with the high cost of rent, franchisees will not be able to be financially viable if the ownership is limited to one or two stores."

As this form of master franchising resembles closely to an area development franchise, the findings suggest that it is preferable that the Asian partner is a business or conglomerate corporation, rather than an individual. It is important that the local partner possesses the financial and administrative resources to build and manage a multi-unit operation. However, caution must be exercised by the international franchisor as the balance of power in the franchisor-franchisee relationship in this case may perhaps be tilted toward the franchisee.

The study found that all the stores of Dome, The Body Shop and CBTL were located at high traffic, high visibility locations in each Asian market. This suggests that it is important for an international franchisor to work with an overseas partner in East Asia who is able to access premium sites, especially for the early ones. As prime retail space is precious and rents are prohibitive, it is important that the foreign partners have real estate contacts and financial strength to undertake such a task. One reason may be that in most Asian countries, the cities are the main centers where tourists, expatriates, youth and professionals go to for shopping, socializing and entertaining.

In contrast, the failure of RCIC at most of its Asian markets was due to wrong locations. The joint managing director claimed: "We had no choice with the locations of two stores, which were to be the showcase to attract franchisees. Our master franchisee told us that they had already got the locations and they had to build them...they were all wrong locations."

Strong market positioning by the western fast food restaurants has been found to be one of the key factors for success in East Asia (Love 1995; Watson 1997; Wee 1997). This is

illustrated by examining the introduction of KFC and McDonald's in Hong Kong (Lan and Khan 1995). KFC opened the first store in Hong Kong in 1973. Within a short span of 12 months, the firm added 10 units. However, two years later KFC closed down all 11 units and withdrew the concept from Hong Kong. It was attributed to a combination of poor locations and uncertain market positioning and pricing.

The study found that the two successful firms namely Dome and CBTL had very clear ideas of what their target markets or niches were. Dome's positioning was "expensive and exclusive" as its target market was the professionals, managers, executives and businessmen (PMEBs). CBTL targeted the youth market, who are the teens and working adults in their twenties. The Body Shop is positioned as "an international brand and possesses a prestige brand image." In contrast, there was little mention of market positioning or target market by RCIC.

Partnership Management

Franchising provides a unique organisational relationship in which the franchisor and franchisee each bring important qualities to the business or partnership (Falbe and Dandridge, 1992). The franchise system enables the advantages of a proven business format offered by the franchisor and the local knowledge of the franchisee to join together (Stanworth, 1995). Their joint contribution and interdependence have made franchising a very powerful form of organisational structure.

All the firms were found to use master franchising as a means to enter markets in East Asia. Therefore it becomes critical for a franchisor to identify the master franchisee characteristics that are required for success in East Asia. There have been several studies conducted in determining desired franchisee characteristics (Anderson, Clarence and Dunkelberg, 1992; Hing, 1995; Knight, 1986; Stanworth, 1995; Withane, 1991). However, no research has hitherto been done, especially in East Asia, on determining master franchisee characteristics. The published articles on this matter tend to be mostly of the trade magazine variety. The study found that the master franchisee characteristics associated with success in East Asia are financial strength, entrepreneurial and like-mindedness.

Although the Body Shop relied on unsolicited enquiries in its early days, it is currently pursuing a more aggressive approach to attracting franchisees. As the competition within the natural, environmentally friendly cosmetics and toiletries market becomes increasingly intensified, there is a need for the firm to be more selective in attracting more experienced and higher quality operators.

The firm's head of franchise explained: "In the early days, the Body Shop was considered an alternative business and therefore we were in secondary locations and didn't cost too much. However, the firm is sited at all the prime locations and therefore there is a need for a financially stronger player."

Variations in cultural norms such as power distance, Confucian dynamism, and individualism can affect local implementation by international firms. Studies conducted by Hofstede (1980) suggest that Asian managers, as opposed to their Western counterparts, are large power distance, weak uncertainty avoidance, collectivistic, moderately masculine, and long-term orientation individuals. For instance, the foreign franchisor may be task-oriented and favor quick results, while the Asian master franchisee has a long-term view and is more oriented towards building a long-term relationship with the franchisor. Such cultural differences will likely create tensions and increase the probability of conflict between the partners. Successful franchising in East Asia, therefore, requires both an understanding of the business and the partners' cultures.

All the firms, except for RCIC had representatives based in Singapore who have extensive knowledge of business practices in East Asia who act as "a conduit between the franchisor and master franchisees." The RGM of Dome is a Singaporean who is a highly experienced manager with an intimate knowledge of the Asian culture. He considers this as an important lesson for foreign franchisors when dealing with master franchisees in East Asia. Due to cultural differences, the foreign franchisor is often regarded by the master franchisee never to

fully understand the intricacies of the Asian culture. Therefore, most franchisor's ideas, policies and suggestions are viewed as questionable in their application to the local market environment.

When the regional head of franchising of the Body Shop was asked on managing partners in Asia, he said: "It is about relationship and therefore you have to spend more time with them than in Europe. In the West, you can get on with the business but in Asia, they don't really tell you what they are thinking as they are not confrontational, therefore you have to spend a lot of time with them to find out what it is."

CONCLUSION

The key aim of this study was to determine the critical success factors of international franchising in East Asia. The key factors within each category are listed in Table 1 to show the areas of activity that must be performed by both potential and current international franchisors to achieve success in East Asia. For potential overseas firms, the findings provide valuable lessons on the requisite capabilities and resources that are needed to achieve financial success when expanding into East Asia. As for current players, the findings allow benchmarking to measure themselves against successful franchises operating in this region. Without a systematic exploration of the critical success factors of international franchising in the region and their impact on performance, most franchisors will have no guidance as to how best to approach and compete in the region.

There clearly needs to be more research performed to further investigate and validate the categories and factors within the categories for successful international franchising in East Asia. Based on the findings of the cases studied, I would like to recommend several directions for future research. Firstly, further inductive studies, involving various franchisors competing in a specific industry (e.g. bookstores, fast-food restaurants, personal service, etc.) or country (e.g. China, Singapore or the Philippines) can be carried out to check on the scope of the categories and factors. Such an exercise would add to the robustness and validity of the findings. Secondly, comparisons of case study analysis of franchisors of different origins in a specific geographical region can be made (e.g. North Asia, East Asia or Southeast Asia) or country (Japan, Indonesia or Malaysia). Such comprehensive studies would provide valuable insights into the different competitive strategies employed or competitive advantages enjoyed by different franchisors (say between a Singaporean and an Australian franchisor). Finally, the findings serve as a useful platform for hypothesis testing using quantitative techniques to validate the correlation between the categories and factors. Following this, multivariate data analysis can be used to determine if there exists any relationship between these factors and firm's performance. This would allow researchers to draw more general conclusions.

Table 1 Critical Success Factors of International Franchising in East Asia

| Category | Key Factors |
|------------------------------|---|
| Distance Management | <ul style="list-style-type: none"> • Must have adequate resources to provide control and monitoring system to ensure product consistent and quality. • Must have a detailed audit and reporting system to control and monitoring the overseas operations. • Must have adequate resources to provide local field support. • Must have the resources and capabilities to manage key staff of master franchisees. • Must communicate regularly with the master franchisees. • Must have the resources to provide initial and continuous training in both home and foreign markets. |
| Contract Enforcement | <ul style="list-style-type: none"> • Must have a solicitor who specialises in international franchising law. • Must ensure that intellectual property is well protected when operating in East Asia. • Must work very hard to achieve success quickly in the early markets to gain the power to negotiate with future master franchisees. • Must possess a high level of proprietary capabilities to reduce franchisee opportunism in East Asia. |
| Cultural Adaptability | <ul style="list-style-type: none"> • Must have clear brand and product policies that are strictly adhered by all master franchisees. • Must work closely together with master franchisees in East Asia to make limited adaptations to the business format and products to suit local market needs. • Must monitor closely the product modifications and innovations introduced by the master franchisees to maintain the integrity of the concept. |
| Host Country Risk Management | <ul style="list-style-type: none"> • Must work with master franchisees who have the capability to undertake evaluation of foreign country government policies. • Must develop a cost effective system of managing exchange risk, which is uncomplicated to administer and understand. |
| Marketing Approach | <ul style="list-style-type: none"> • Must progress from master franchising to joint ventures as international experience and resources grow to gain greater control and financial returns. • Must have franchised stores situated at premium sites in East Asia. • Must work with master franchisees who have the financial means and/or contacts to access premium sites. • Must have clear market positioning in East Asia. • Must have the capabilities to undertake niche marketing in East Asia. |
| Partnership Management | <ul style="list-style-type: none"> • Must adopt a more aggressive proactive approach in recruiting potential master franchisees. • Must have master franchisees who possess the characteristics of financial strength, entrepreneurial and like-mindedness. • Must demonstrate a commitment to establish a long term working relationship with the master franchisees in East Asia. • Must have a manager who has an intimate knowledge of East Asian culture as a local representative. |

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APPENDIX A: GUIDELINE FOR INTERVIEW QUESTIONS

Distance Management

1. How do you control and monitor your franchisees' performance?
2. What difficulties have you faced in managing your franchisees in Asia?
3. What support do you provide your franchisees in Asia?
4. How often do you communicate with your franchisees in Asia?
5. What sort of information do you communicate with your franchisees?

Contract Enforcement

6. Who are involved from both sides during the negotiations?
7. What were the major issues considered during the negotiations of the franchise agreement?
8. How different is the international franchise agreement compared to the domestic one?
9. Did you face any difficulties in negotiating with the Asian partners?
10. How much are the franchise fees, royalties and levies?
11. Have you experienced any difficulties in enforcing the contract with the Asian partners?
12. Have you experienced any difficulties in the protection of the company's intellectual property in Asia?

Cultural Adaptability

13. Do you practice adaptation in Asia? Why and what are they?
14. How do you know how much to adapt in Asia?
15. How do you know if the adaptation will work?
16. What resources do you have in managing adaptation and innovation?
17. Are there any other cultural issues that would require adaptation of the business?

Host Country Risk Management

18. Did you evaluate foreign government policies before you entered the market? Why or why not?
19. What were the foreign government policies you evaluated?
20. What resources do you have in evaluating foreign government policies?
21. How do you manage foreign exchange risk?
22. Are there any other issues in managing the risk of entering overseas market?

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Dr Alan Nankervis
School of Management
Curtin University of Technology
GPO Box U1987
Perth Western Australia 6845
Telephone: + 61 8 9266 7413
Facsimile: + 61 8 9266 7897
Email: nankerva@cbs.curtin.edu.au

SCHOOL SECRETARY

Ms Tonia Geneste
School of Management
Curtin University of Technology
GPO Box U1987
Perth Western Australia 6845
Telephone: + 61 8 9266 7292
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