

SA study of the Factors of Chinese Franchisor's Re-contract

Shuai Su*

Abstract

Purpose - The objective of the paper is to explain the factors affecting on the Re-contract intension of franchisor in the uprising Chinese franchise market.

Research design, data, methodology - The study conducted a survey on the 400 franchisors data in China from January to July 2012. By AMOS analyzing the data to examine these hypotheses empirically, we can confirm most hypothesis supposed.

Results - This study shows that the high management performance and satisfaction of the franchise headquarters has a positive effect on the Re-contract intention of franchise. In the case of large markets such as China, the franchisor's strategy and the role is very important.

Conclusions - This study provides franchisors and practitioners, who plan to extend their franchising business abroad into Chinese market, with some practical knowledge. In order to achieve stable profits, the franchise corporation needs to support the operation of the individual franchisee through incentives and standardization of services.

Keywords : Chinese franchise market, re-contract.

JEL Classifications : M31, M12, F23.

1. Introduction

Recently, there are about 100 franchise stores in the US. These chain stores make one trillion profit every year. The jobs, more than one thousand and one hundred, associated with franchise industry have been accepted as a common definition in the US. Moreover, the Japanese franchise industry has made 1,720 hundred millions profit in 2007. The 230 thousand chain stores have formed a huge market in this field. In Korea, in the end of 2008, the franchisor were 2,426, and the number of franchisees were about 257,274. In addition, the employees were one billion, and it has took 10.4% GDP with 97 trillion won in this market. It has spreaded into 250 different service in-

dustries such as food service industry, retail industry, educational institution, care center, beauty salon. And the franchise system was carried out by the government. As a result, by 2012, the 8.6% of the total GDP, 113 trillion, the rate of service is increasing by 18%. It is expected that the growth of franchise industry will be active. Now the industry of franchise has become one of the fastest developed industry in the world. This development has brought a ripple effect.

This research is going to find out the factors affecting the Chinese franchise system and analyze the recent develop situation and problems. Especially, this study is to analyze the factors influencing the recontract of franchise growth in China. In detail, this research analyze how the factors such as the characteristics of franchisor, franchisee, the relationship between franchisor and franchisee, environment influence the relationship between the Chinese franchisor and franchisee. Furthermore, most literature focus on franchisor to study recontract. However, this research focus on franchisor to find out how factors are important. This study contributes to the intranational franchise companies for making effect strategy to enter the Chinese market.

2. The Chinese Franchise Development

From 1990s, the Chinese franchise industry has developed quickly. After 2001, the demand of new service has been increasing. According to the Chinese chain business association, by the end of 2011, the number of franchisor in China is about 5000, and the franchisee is more than 300 thousand. The performance of the TOP 120 franchisor is more than 3730 hundred million RMB, the rate of service is increasing by 9.6%. Among these industries, the food, retail franchise industries are the most ones. It has found that 31 companies of the 120 Chinese chain companies are the food hotels. Among those hotels, 11% are the foreign brand, and the franchisors are opened in the capitals such as Beijing, Shanghai, Guangdong Provinces. After opening the door, the economy has developed quickly. According to the report of the China Chain Store & Franchise Association, there are 6 companies in the TOP 10 that have made the profit over 100 hundred million RMB. Among the TOP 120 franchise companies, the listed companies have been 24. And in all TOP 120, there are about 80% companies are going to enter the listed companies. Furthermore, there are 66 (55%) companies of the TOP 120 ones use franchise systems to operate the companies. In addition, in the future, there are 14% companies plan to use kinds of brand system to operate the companies. In each local, there are 8 areas such as Beijing, Tianjing, Shanghai, Shenzheng and the cities around Bohai, East and South of China are the highest in

* This paper has been represented by KODISA 2012 Summer Conference. Reviewed by new data examiners.

** Corresponding Author, Professor, Shandong University of political science and law, China. Tel: 86-156-6582-3837. E-mail : su.shuai@gmail.com

income and consumption culture. According to China Chain Store & Franchise Association. Most of the franchise stores are dispersing around Bohai, East and South China, and Southwest. Furthermore, most of these franchisestores are in Beijing, Shanghai, Guangzhou, Tianjing, Hangzhou. The income and the consumption levels are higher than other cities. Among these cities, most of the franchise companies are operated by food service, retails, healthcare and cosmetic treatment. In 2009, the franchise industries can be divided by wholesales-retails (40%), food service (30%), and service industry (26%). Currently, a new product and service which is different from the past franchise system is entering the market. As a result, the franchise associated with service will be increasing quickly.

The concept of franchise in China did not exist from 1984 to 1992. And it is difficult for the foreign companies to enter China due to the govern control. The foreign franchise industry started with the opening of KFC in Beijing in 1987. After 2000, the franchise industry was developing quickly, and from 1st Feb., 2005, the foreign franchise industry developed in China with a large-scale. Now the franchise brand is increasing with the door opening of retails and services. Currently, the foreign franchise in the Chinese market are focusing on the high level consumption as the target through well-being, different service, luxury. Take the clothes as an example, Jean George, Send & Bund, Face Bar are the main restaurant. There are 112 Carrefour stores in China, and the profit is the first one with 296 hundred millions yuan. In addition, KFC, TACO BELL, Pizza Hut, Long John Silver's are operating 35,000 restaurants. These brands make 215 hundred millions yuan every year which are the first one in the food service industry. And now, among the foreign franchise brands in China, the American ones take up 50%. According to the Franchise Times "the 200 franchise companies in 2004" in America, there have been 60 franchise brands entering China. Especially, 14 (65%) brands of the 20 franchise brands in them have developed in China

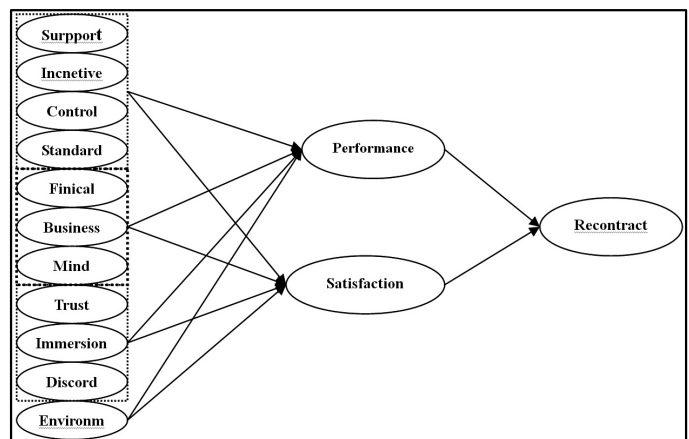
3. Research Model and Hypothesis Development

The factors influencing franchise system performance have been studied by lots of scholars. However, most of the studies only focus on franchisor characteristics, franchisee characteristics, and the relationship characteristics and competitive characteristics between franchisor and franchisee to find out how they influence the performance. Stern & El-Ansary (1988) estimate the effect of service support by franchisor on performance. Hoffman & Preble (1991) explain the impact of organization management and operation direction standardization on performance. Smith (1993) find out the effect of communication, training, problem solution, and support while Morgan & Hunt (1994) insist the franchisor support is important for the performance.

In addition, there are a lot of researches of the impact of franchise characteristics on performance. Doutt (1984) find out the importance of fund status, store size and the number of employees of the company profit. Especially, Lussier (1996) explains the effect of funds management. Shan (1997) studies the impact of businessman mind,

business experience and store location covariance on performance. Currently, Han (2009) find out the impact of franchisor disposition, in other words, business management ability and operation cost on profit. There are lots of studies of the relationship between franchisor and franchisee influencing franchise system performance. Lusch (1976) find out the impact of discord between franchisee and franchisor on performance. Morrison (1997) and Kim (1994) estimate the effect of discord and trust and immersion on profit. In addition, there are also studies of market competitive and franchise environment characteristics influencing performance. Campbell, Datar, & Sandino (2007) focus on the market environment to study performance. Kim(2006) explain the impact of market environment movement. And Kim and Bek (2008) find out the effect of uncertainty of demand. Hussain, & Windsperger (2010) analyze the impact of environment risky on performance. Recently, scholars put franchisor characteristics, franchisee characteristics, the relationship between, and the competitive characteristics together to modelling the their impact on performance (Shin 2000; Kim 2003; lee 2010). However, most of these research focus on franchisee to study the impact on performance. It is because focusing on franchisor to do such research is difficult. This study is going to find out how these factors influencing performance with the background of franchisor. Especially, we collected data in China to find out how franchisor characteristics, franchisee characteristics, the relationship between franchisor and franchisee, and environment characteristics influencing franchisor profit.

In this research, the factors influencing performance are based on the literature. In order to find out the impact of franchisor characteristics, franchisee characteristics, the relationship between franchisor and franchisee, and environment characteristics on performance, the research model was made <Figure 1>. Furthermore, franchisor profit can be constructed by business profit, the satisfaction of franchisor stores, and the recontract between franchisor and franchisee in the future. In another word, this study not only analyze the impact of franchisor characteristics, franchisee characteristics, the relationship between franchisor and franchisee, and environment characteristics on performance, but also how these factors influencing the evaluation of franchisor to franchisee and satisfaction. Finally, this research find out how they affecting the recontract relationship between franchisor and franchisee.



<Figure 1> Research Model

According to the research model, we display the hypothesis as follows. At first, the activities of franchisor, the support to franchisee, incentive, control, system standardization are significantly associated with the profit of franchisor.

- H1: The support of franchisor significantly (+) influences the business profit of franchisor.
- H2: The incentive of franchisor significantly (+) influences the business profit of franchisor.
- H3: The control of franchisor significantly (+) influences the business profit of franchisor.
- H4: The system standardization of franchisor significantly (+) influences the business of franchisor.

And it is predicted that The final ability, business ability, businessman mind are significantly associated with the business profit of franchisor and the satisfaction of franchisee stores.

- H5-1: The good final status of franchisor significantly (+) influences the business of franchisor.
- H5-2: The good final status of franchisor significantly (+) influences the satisfaction of franchisee.
- H6-1: The business ability of franchisor significantly (+) influences the business of franchisor.
- H6-2: The business ability of franchisor significantly (+) influences the satisfaction of franchisee.
- H7-1: The good mind of franchisor significantly (+) influences the business of franchisor.
- H7-2: The good mind of franchisor significantly (+) influences the satisfaction of franchisee .

In addition, it is predicted that the relationship such as trust, immersion, discord between franchisor and franchisee are significantly associated with the business profit of franchisor and the satisfaction of franchisee .

- H8-1: The trust(franchisor/franchisee) significantly(+)influences the business of franchisor.
- H8-2: The trust significantly (+) affects the satisfaction of franchisee.
- H9-1: The immersion(franchisor/franchisee)significantly (+) influences the business of franchisor.
- H9-2: The immersion significantly affects the satisfaction of franchisee stores.
- H10-1: The discord(franchisor/franchisee)negatively (-) influences the business of franchisor.
- H10-2: The discord negatively (-) affects the satisfaction of franchisee stores.

It is predicted that the uncertainty of business environment such as the likelihood change of consumer, the sales of competitive company, and the strategy change of ad., are negatively associated with the profit of franchisor.

- H11: The uncertainty of business environment negatively (-) influences the business of franchisor.

It is predicted that the better the profit of franchisor the better satisfaction of franchisee. As a result, the decision to recontract between franchisor and franchisee will be higher.

4. Data collection and analysis method

4.1. Questionnaire construction and the concept of variance

According to the literature, this research made the questionnaire. The operating definitions of each variable are constructed by 15 variables with 67 items.

4.2. Data collection

According to the Chinese franchise association, we collected the data from the main cities, Beijing, Shanghai, and Guangzhou in China from 15th Jul. to 15th Aug., 2010. There are 4,000 franchisor in these cities. In order to improve the reliability of the data, we depended on the professional research association in China to collect the data from 398 franchisors. With the data, we use AMOS to analyze the data. In addition, Cronbach's alpha analysis is used to confirm the reliability of each variable.

5. Results of reliability and validity

Cronbach's Alpha analysis is used to test the reliability of each variable. Some of the items in each variable are deleted. As a result all variables' Cronbach's Alpha are more than 0.7. As a result of the confirmatory factor analysis, we use the factors to do the deep analysis. And the factors can be concluded as follows: franchisor characteristics, franchisee characteristics, relationship characteristics, environment characteristics, franchisor satisfaction, franchisor business performance, franchisor recontract intention. Each Alpha of the factors are more than 0.7, thus the reliability is high. Structured Equation Model (SEM) is used to test the validity of the research model. The model has a good fitness ($GFI > 0.9$, $0.05 < RMSEA < 0.06$). The results of reliability and validity are shown. All the factor loadings are more than 0.5. Thus, the reliability and validity are higher.

6. Analysis results of hypothesis

In order to test the research model, AMOS 17.0 is used to do the path analysis. The research model has good fitness ($\chi^2=1,568$, $p < 0.000$, $GFI=0.903$, $AGFI=0.877$, $RMSEA=0.065$). The results are given in Tables 1 .

<Tables 1> The results of hypothesis

		Path	Standardized coefficient	T-value	P-value	Accept or Reject
H1	Franchisor's characteristics	H1-1 Support→Performance	0.194	3.306	0.000	Accept
H2	Franchisor's characteristics	H2-1 Incentive→Performance	0.137	3.239	0.001	Accept
H3	Franchisor's characteristics	H3-1 Supervisor→Performance	0.103	1.63	0.103	Reject
H4	Franchisor's characteristics	H4-1 Standardization→Performance	0.219	4.08	0.000	Accept
H5	Franchisee's characteristics	H5-1 Finance→Performance	0.11	2.5	0.010	Accept
H5	Franchisee's characteristics	H5-2 Finance→Satisfaction	0.285	5.527	0.000	Accept
H6	Franchisee's characteristics	H6-1 Management→Performance	0.136	2.584	0.020	Accept
H6	Franchisee's characteristics	H6-2 Management→Satisfaction	0.263	4.236	0.000	Accept
H7	Franchisee's characteristics	H7-1 Entrepreneurship→Performance	0.124	2.236	0.020	Accept
H7	Franchisee's characteristics	H7-2 Entrepreneurship→Satisfaction	0.451	7.728	0.000	Accept
H8	Relational characteristics	H8-1 Trust→Performance	0.086	1.938	0.053	Accept
H8	Relational characteristics	H8-2 Trust→Satisfaction	0.053	0.886	0.376	Reject
H9	Relational characteristics	H9-1 Commitment→Performance	-0.02	-0.349	0.694	Reject
H9	Relational characteristics	H9-2 Commitment→Satisfaction	0.097	1.607	0.108	Reject
H10	Relational characteristics	H10 Conflict→Performance	-0.447	-2.268	0.007	Accept
H10	Relational characteristics	H10 Conflict→Satisfaction	-0.066	-0.959	0.337	Reject
H11	Uncertainty	H11 Uncertainty→Performance	-0.321	-1.952	0.051	Accept

Franchisor characteristics such as franchisor support, incentive and system standardization significantly (+) influence franchisor performance. This is consistent with the research by Shin (2000), Kim (2008). Thus franchisor should not focus on franchisee employment. Franchisor should focus on the factors influencing performance such as system standardization and incentive to make strategy. However, the hypothesis of franchisor control is rejected. It is because the Chinese market is so big and the business environment is complex. According to the different economy, it can be divided into east area and west area. Thus, it is difficult to do franchisor control by one evaluation standardization.

The factors of franchisee characteristics, franchisee financial, franchisee business ability and businessman mind are associated significantly (+) with franchisor performance and satisfaction. This result has been confirmed by Lussier (1996), Han (2009). And the result of franchisee financial, business and business ability and businessman mind influencing satisfaction is consistent with the research by Weaven & Franzer (2007), Kim (2009). Thus, it is important to consider franchisor financial, business ability and businessman mind when franchisor choose the chain stores.

Among the relationship between franchisor and franchisee, the trust between them is significantly associated with performance. The dis-

cord has a negative effect. These results are consistent with the results by Pavlou & Ba, 2000; Morrison, 1999; Weaven & Frazer, 2007. However, these factors have no effect on franchisor satisfaction. Thus, it is because the status of franchise system in China is so big.

Finally, environment change and uncertainty have negative (-) impact on franchisor business performance. This result has been confirmed in the literature research (Campbell, Datar, & Sandino, 2007). Generally, when the market is changing and uncertainty, they will influence the franchisee negatively. Thus, it is necessary to make strategy for improving the certainty. Finally, franchise business performance and satisfaction is significantly associated with the recontract of franchisee. The better the business performance and the higher satisfaction of franchisee, the higher possible the recontract with franchisee.

7. Conclusions

The franchise industry is developing quickly in all the world. It has brought extent effect in the national country. After China entering WTO in 2004, all the wholesale retailers have opened. And the franchise industry developed quickly. Even though, there are only 20 years history of franchise in China, it has been the largest franchise market in the world. However, research of the Chinese franchise market is scarcity. From 1990, the International Franchise Association (IFA) and some researchers focus on China and Europe to do the research. However, they only focus on investment in the Chinese market. Thus, it is difficult to understand the culture, economy and society market environment of the Chinese franchise industry. There are researches in national China, but the research of franchisor is scarcity. Thus, the effect of franchisor in China is great. It is because it is necessary to make different strategy in each area. This researches focus on franchisor strategy, franchisor characteristics and relationship with franchisee to find how they influence franchisor business performance, satisfaction, and recontract intention.

Thus, the factors influencing franchisor performance, franchisor characteristics such as franchisor support, incentive and system standardization are significantly (+) associated with franchisor business performance. Among franchisor characteristics factors, franchisee financial, businessman ability and business mind are significantly (+) associated with franchisor performance and satisfaction of franchisee. Among the factors of relationship between franchisor and franchisee, trust has a significant (+) effect on performance. And the discord has a negative (-) influence on performance. However, trust, immersion, and discord have no effect on satisfaction of franchisor. Environment uncertainty is negatively (-) associated with franchise performance. Finally, the higher the business performance and satisfaction, the higher recontract intention is. However, this research has some limitations when finding the impact of factors on franchise recontract. First, among the factors of franchisor performance and satisfaction in this research, the impact of franchisor characteristics, franchisee characteristics, relationship characteristics, environment characteristics are confirmed. However, other factors influencing franchise performance and satisfaction are not confirmed. Thus, in the future, it is necessary

to find the effect of other factors in this research model. Second, the data is collected from Beijing, Shanghai, Guangzhou in China. Thus the result of this research is difficult to be generalize. Thus, it is interesting to get more data to compare the different industries. Finally, this research only collected the data of the franchisor, not the data of franchisor and franchisee. Thus, it is interesting to collect the data of franchisor and franchisee to study the factors influencing the decision-making in the future.

Received: October 29, 2012.

Revised: December 17, 2012.

Accepted: December 17, 2012

References

- Hoffman, R. C. & Preble, J. F. (1991), "Franchising: Selecting a strategy for rapid growth", *Long range planning*, 24(4), 74 - 85.
- Huang, Chin Hsuan (2008), "investigating relationships between relationship quality, customer loyalty and cooperation: an empirical study of convenience stores' franchise chain systems in taiwan" PD paper.
- Hussain, D. and Windsperger, J. (2010), "Multi-unit ownership strategy in franchising: Development of an integrative model", *Journal of Marketing Channels*, 17(1), 3~31.
- Kaufmann, P.J. and Dant, R.P. (1996), "Multi-unit franchising: Growth and management issues", *Journal Business Venturing*, 11, 343-358.
- Lussier, R. N. (1996), "A business success versus failure prediction model for service industries.", *Journal of Business and Entrepreneurship*, 8(2), 23-37.
- Morgan, R. M. and Hunt, S. D. (1994), "The Commitment-Trust Theory of Relationship Marketing", *Journal of Marketing*, 58, 20-38.
- Morrison, K. A. (1997), "How franchisee job satisfaction and personality affects performance, organisational commitment, franchisor relations, and intention to remain", *Journal of Small Business Management*, 35(3),39-67.
- Roh, Eugene, Y. & Yoon, Ji-Hwan (2009), "Franchisor's ongoing support and franchisee's satisfaction: a case of ice cream franchising in Korea", *International Journal of Contemporary Hospitality Management*, 21(1), 85 - 99.
- Stern, L. W. & El-Ansary, A. I. (1988), *Marketing Channels* (3rd ed.), Englewood Cliffs, New Jersey: Prentice Hall.
- Vázquez, Luis (2008), "The choice of control devices in franchise chains", *The Service Industries Journal*, 28(8), 1093-1105.
- Weaven, S. and Frazer, L. (2003), "Predicting multiple unit franchising: a franchisor and franchisee perspective", *Journal of Marketing Channels*, 10(3), 53-82.
- Weaven, S., and Frazer, L.(2007), "Mature franchise systems use multiple unit franchising to leverage learning economies and sustain system wide growth. Asia Pacific", *Journal of Marketing and Logistics*, 19(2), 107-126.