BIZCOMMUNITY

Franchise proves winning formula

Richemont opened nine more franchises last year. The world's largest producer of luxury products, with brands such as Cartier, Jaeger LeCoultre and Montblanc, also opened 20 more company-owned retail outlets.

The move, which brings the company's total of franchises to 582 and stores to 817, came as it cut sale agreements with third-party retailers in an effort to gain better control over the sale of its goods, a spokesman said last week.

Franchise works well in retail, whether the product is a high-end watch or a basic burger. It works in any operation where a formula can be replicated easily. As with Richemont - which has seven franchised stores in SA and one company-owned store - many companies have a mix.

All of Famous Brands' 1779 stores - including Wimpy, Steers and Mugg & Bean - are franchised.

About 60% of McDonald's 135 stores in SA are franchised and 40% are corporate-owned.

Scope for growth

Companies change the mix according to their needs. Franchising carries its risks, but offers rewards. In SA today, however, it remains small. Just 12% of retail sales here go through franchises. In the UK, the figure is 30% and in the US, 52%.

"We obviously still have scope for growth," says Anita du Toit, of First National Bank's franchise lending division.

Franchising allows cheap expansion. Franchisees, rather than companies, bear the costs of new stores. Companies often go for franchises in marginal areas, opting for a lower, but guaranteed return from franchise fees, rather than a return on the store itself.

Supermarket chain Pick n Pay opens its first store in Zambia, a franchise, on Thursday. It has signed up franchise partners for its planned expansion into Mozambique and will expand into Mauritius in the same way.

Profitability

Taste Holdings, the listed company behind Scooters Pizza and Maxi's restaurants, owns just four of its 190 food outlets. The mix has changed from the early days, when Taste owned 13 of its 40 stores. Back then, it needed the store revenue.

"Franchising is only profitable when there are a number of stores. If you only have franchise royalty, the breakeven is a good two to three years away," Taste CEO Carlo Gonzaga says.

Importance of marketing

In the food business, marketing is crucial. An advantage of franchising, Gonzaga says, is that the marketing fee each store pays allows a bigger promotional spend than would otherwise be possible. It does not just apply to food. Taste also owns 21 of SA's 80 NWJ jewellery stores, while the rest in the chain it controls are franchised.

"We are the only franchised jewellery chain. We spend more than double our nearest competitor in marketing, because we've got more money," says Gonzaga.

Still, his goal is to reduce the overall proportion of franchises.

"We will probably in a couple of years start buying back stores."

Different strategies

McDonald's is going in the opposite direction. The McDonald's pattern in the US and Australia is 70% franchise, 30% corporate and as the number of stores in SA grows - with a 10%-15% increase in store numbers a year - that ratio will change, McDonald's SA MD Greg Solomon says.

There is a different pattern at Roman's Pizza, a Centurion-based family company with 116 stores. MD John Nicolakakis says 8% of stores are corporate, 48% are franchised and 35% are joint ventures between the company and partners.

These hybrids give head office more control in an operation that is strategically important, or run by someone who may not have had the necessary start-up capital. This model, rather than franchise, is Nicolakakis's preferred way of growing.

Brand damage

While a good franchise is the biggest asset to a business, a bad one is the worst asset you can have. "It can do a lot of damage to your brand," he says.

The quest for control in the food industry, where the potential for damage is great, leads to much tweaking of the ownership model. Another Roman's strategy is to have stores run by "operational partners". These are managers who benefit directly from the store's profit but do not have equity. Taking a different line, Taste, in an effort to retain control of key sites, keeps the leases and sublets the site to the franchisee.

"I don't think there's one right answer," Gonzaga says. "It depends on your strategy."