

Development of franchising in Bulgaria in the period after the crisis

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Abstract

Franchising is an extremely followed business strategy in the contemporary world of competitive companies on a global level and in Bulgaria. Like any other business it also has its positive and negative sides. It builds enviable business relationships between the entrepreneurs. Moreover their businesses work together in a symbiotic way as interdependent and indispensable to one another. Over the years, however, this privilege called franchise has changed constantly in commercial environments.

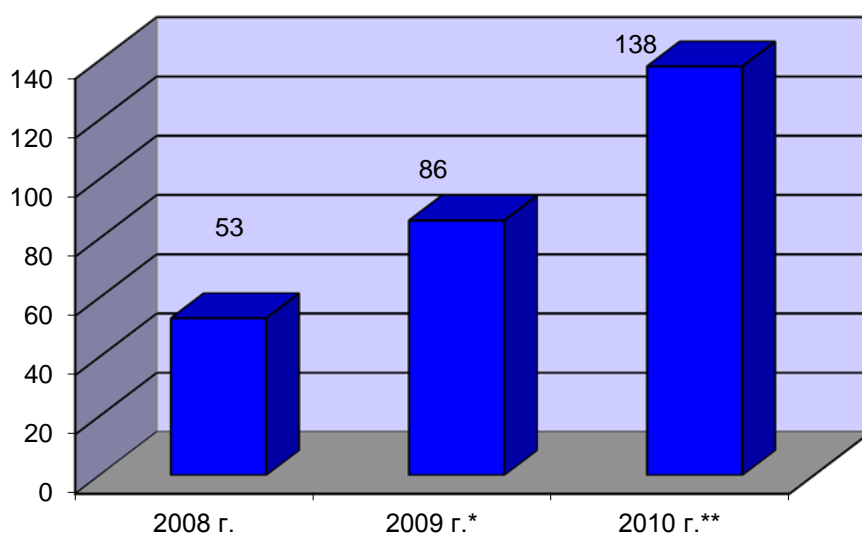
Key words: *franchising, crisis, business strategy.*

Nowadays, the concept of franchising is getting more and more popular. But what exactly is it? This is a contract-regulated distribution scheme of products and services between a franchisor and a franchisee in which the franchisee takes advantage of already proved business model, complies with it and pays taxes. The following of this scheme shows that almost every product and service could be offered by means of franchising. Worldwide franchises are most highly developed in services and nutrition. According to the standard, the financial parameters of a franchise include an initial fee and monthly royalty deductions, usually determined as a percentage of turnover. Basically, franchise systems are very different as the initial franchise fee could be 2000 or 200 000 Levs, or it could not have one. In Bulgarian conditions, for the lack of a high level of financial discipline since 2008 until the present days, it is actual for the percentage of turnover to be formulated as "X% of turnover but not less than Y lev per month." The franchisor may give the franchisee the right to use the trademark, projects, models, management techniques, recipes, formulas, and it is often bound by an obligation to use the

materials, resources and equipment supplied by the franchisor. The purpose of this report is to inform about the development of this highly reliable business after the financial crisis in the aforementioned 2008 and to show the newly trends of franchise business in Bulgaria.

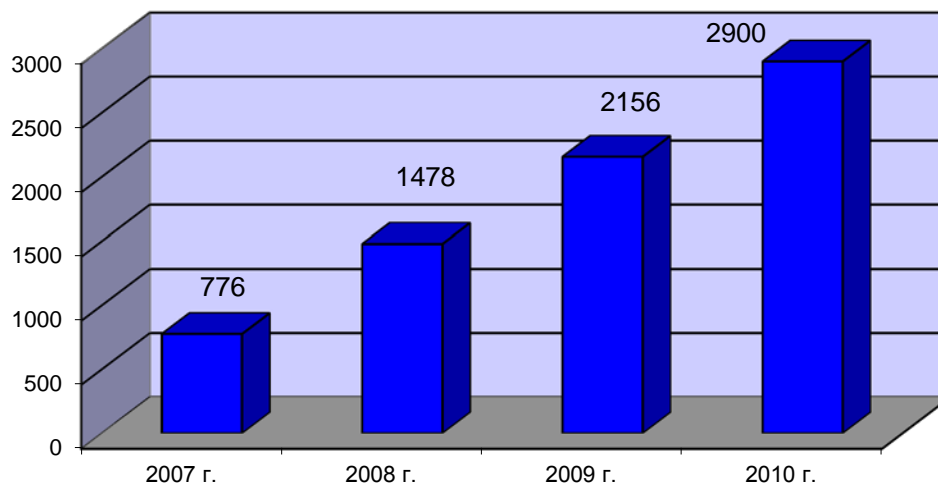
A survey of 34 franchisors and 126 franchisees, conducted between July and September 2009 states that in the last two years the franchise market in Bulgaria is experiencing a real boom. Since the end of 2007 until today, the number of companies offering franchise in the country has tripled. However, at the end of 2008 it was no more than 60. Since the beginning of 2009 until today, more than 20 new franchise systems have started operating in Bulgaria. By the middle of 2009, over 80 systems offer their franchise rights for starting a small and medium business. 62% of them are Bulgarian companies and 68% are in the market for more than five years.

A number of companies offering franchise



By the end of 2007 the number of outlets run by franchise was 776. In 2008, 702 new sites are found, an increase of 90% in just one year. Franchisors expect that at the end of 2009, the outlets in Bulgaria run by franchise will reach 2156 and at the end of 2010 - they will be over 2900. Food industry has the most franchises (over 15) and in the sphere of real estate, franchise business is offered by 7 companies.

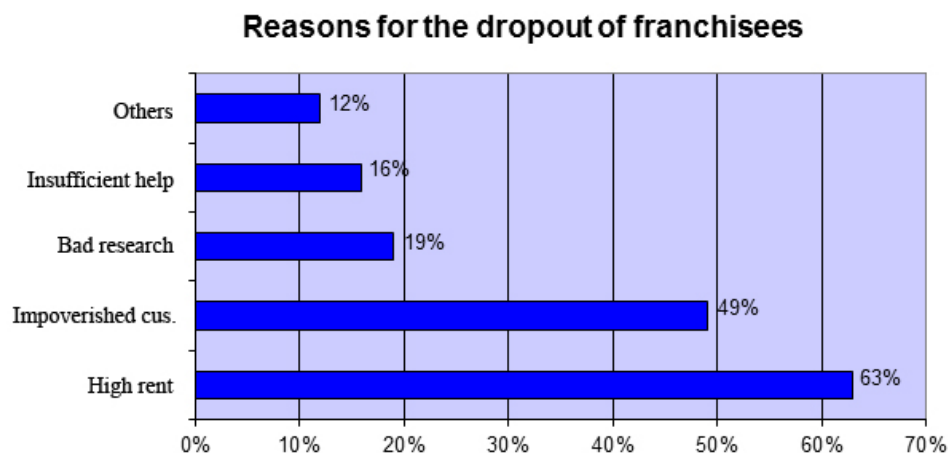
A number of working franchise objects



From January 1 to September 1, 2009, 8% of franchisees dropped out of business. The main reason for the closure of sites is the insufficient capital available to withstand the current turmoil in the market. 63% of respondents specify that the reason for dropping out of the franchise system is high rental costs, which after the deterioration of the economic situation in the country, make business unprofitable. According to 49%, the main reason for that is the decreased purchasing power of customers. 19% feel that they haven't studied the business well before joining it. Only 16% of the dropouts believe that the franchisor did not give them the necessary support, and 12% indicate other reasons (family, health, the appearance of close competitor, etc.) The sum of the percentages exceeds 100 because the respondents gave more than one result.

According to another research at the International Franchise Association (IFA), about 90% of the enterprises which operate under franchise, at the end of their fifth year were still on the market. Although the percentages are not among the maximum 100%, the principle remains - franchising is the safest way to start a new business in Bulgaria.

Another positive aspect of the franchise companies is that they are significantly in favor of employment. In 2008, the objects found by buying a franchise created 2370 jobs in the country. Despite the financial crisis from the beginning of this year to September 1 were found over 3,300 new jobs and the franchising outlets in the country are employing over 8,000 employees at the moment.



Here are some successful examples of development of franchise business in the country:

On June 18, 2007. Angel Dimitrov – the owner of "Branges", opened the first franchise object " Fornetti " in Varna. During this period, the Hungarian circuit is unknown in the country, but it quickly finds partners. In this case the franchisor (producer of frozen snacks) wins by selling their products to the franchisee. The latter, in turn, benefits from the discount in the purchase and the final price which is fixed for all objects in the chain. A. Dimitrov is convinced that "franchising is a successful model in which there is no need to find the hot water, and to work with established rules and products."

Another representative of the entering for Bulgaria franchise is Strahil Strahilov, market development manager in franchise chain stores for second hand clothes Mania. For the past few years, Mania has become a preferred and recognizable brand through its expansive marketing strategy including interesting ideas such as its own radio. Strahilov determines the sign of a successful franchise succinctly: "Happy and satisfied franchisees."

"Average" franchise in Bulgaria

According to a study of Franchising.bg parameters, "average" franchise in Bulgaria for 2012 is:

- Franchise fee - the average of the initial franchise fee is 17 825 Levs There is a trend for franchisors to assume the initial training for their expense which aims to launch their business and carry it out with less investment so that it could be more available for entrepreneurs.

- Monthly "royalty" fees - these are the average monthly charges for Bulgaria, as statistics show that in 2012 they were amounted to 6.2% of a turnover.
- Fee for national advertising fund - when such a charge is demanded, it is usually between 2% and 4% depending on the branch.
- Total investment to start a franchise business - 38 454 Levs
- Number of sites - statistics show that on average, the franchisor in Bulgaria is accounted for 28.4 objects.
- Average contract duration - 4.5 years.

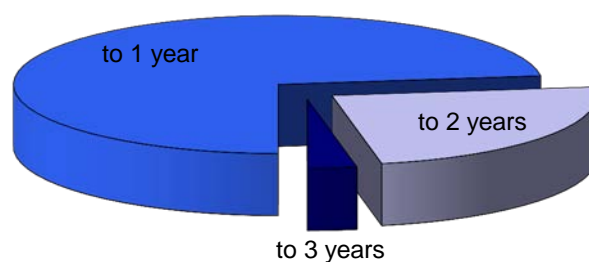
Overall, 73% of franchisees agree with the statement: "The profit from my franchise is greater than the sum needed for the support of my family."

Return on investment

The return on the investment made in starting a franchise business is strictly individual and depends mainly on the skills and efforts of the franchisee. For the period since 2007, the average time for return on investment, after starting a franchise business has been 15 months.

73% of respondents say that the investment in their franchise returns to the end of the first year. For 24% of franchises the investment returns within 24 months, and 3% - within three years.

Deadline for return on the investment in starting a franchise business



These results are one of the main reasons why this franchise is among the most popular options for business in Bulgaria. It offers proved to conduct business and is associated with shorter deadlines and less risks.

Different market sectors are affected differently by the crisis. Depending on the sector, the decrease in the turnover is averaged 10 to 70%. Among the most affected are real estate and other sectors related to buying on credit, and the least - franchises of food sector.

63% of respondents believe that their companies' decline is smaller than that of independent contractors by their industry, who do not operate as a franchise. The main reason for this results in the fact that franchise companies work under a famous brand and offer products with consistent quality. According to 82 percent of those surveyed after the crisis, albeit with lower sales, those who operate as franchisees will have a higher market share because the market will remove some of the independent entrepreneurs.

Franchisors share observations on a clear process of restructure in the economy and many entrepreneurs, from the most affected by the crisis sectors, divert to other branches. They have capital and business but lack of the necessary experience and know-how.

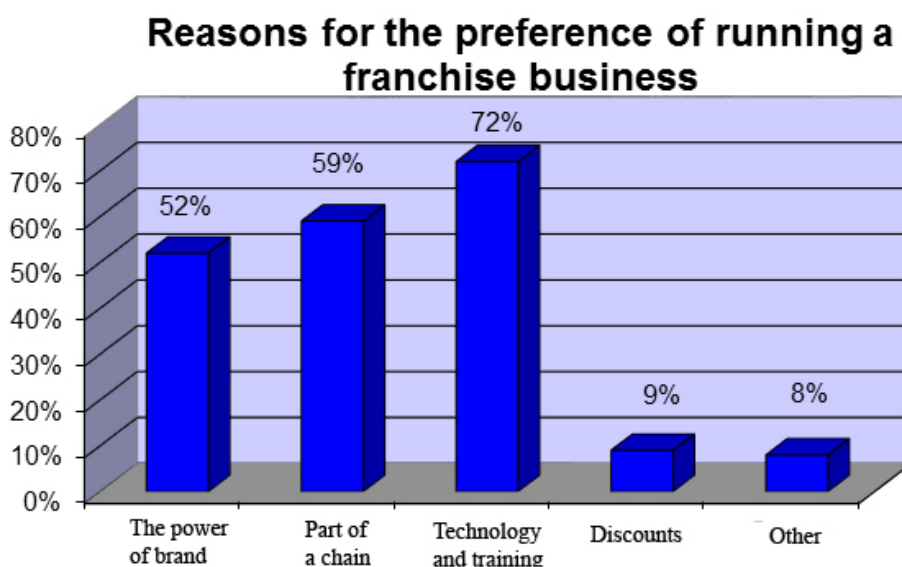
Conversion franchise

The so-called conversion franchise increasingly came into practice in Bulgaria. This is an existing business opportunity to join a franchise system by agreeing to operate under its name, by its rules and pay charges.

Respondents identified as a major problem the lack of credit, which hinders the development of franchise systems – both as an obstacle to business financing and decrease in the solvency of customers. The percentage varies in different sectors, but on average 73% of respondents agreed with the statement: "The crisis will end when the banks start giving loans again."

The economic crisis has a positive influence on the ability to provide employees of the fastest growing franchise structures. This opinion is shared by 82%. The average number of candidates who apply for low-skilled jobs grew almost three times compared to the same period last year.

Many entrepreneurs prefer to franchise instead of starting their own business. This trend is supported by 52% of respondent candidates who say they do it because of the power of the brand, 59% - to be part of a national or regional chain, 72% - because they will receive technology and training, 9% - because it gives them the opportunity to buy goods, materials, advertising, etc. on a discount, 8% - reported other answers. What is interesting here is that our franchisees believe more in "group security" than in the strength of the brand.



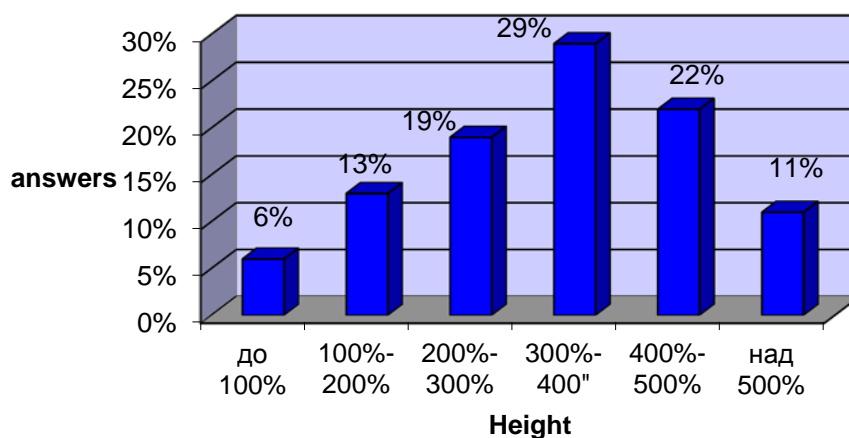
How the new franchise systems appear?

36% of the new franchises that began work in the country during the last 12 months have been "imported" and the remaining 64% are Bulgarian companies which grow their business by offering franchise.

The average amount that the new Bulgarian franchisors invest in developing a new franchise system - operational manual, contract, branding, software, candidates tests, training a franchise manager, promotion of franchise and other administrative costs is 48 000 Levs.

For the period since 2008 – 2012, the share of sales of franchise businesses in the Bulgarian economy grew enormously and this increase varies significantly - from 200 to 500 percent.

Expected sales growth through franchising in the 2008-2012



The greatest problem and the greatest opportunity

Virtually unanimous - 92% of franchisors define our poor knowledge as the biggest problem that the development of franchising faces - the ignorance of the business model and the benefits that it brings.

The greatest opportunity for the development of franchising is the presence of an extremely large number of undeveloped franchise niches - especially in the service and retail sectors there are entire industries which do not offer even a single franchise.

In conclusion we can say a few basic things:

- In a crisis, franchise systems are more stable because of the recognizable brands and constant quality. Therefore by entering into a franchise, the independent entrepreneurs see an opportunity of chain survival.
- The interest in proven business models and brands is increasing, because of the low risk and security they provide.
- The main problem the franchise companies in the country face is the lack of knowledge of the Bulgarian business with the principles of franchising.
- Despite the rapid development, the real boom of franchise business has not come to Bulgaria yet.

There are still many branches that do not work under any franchise system. They have the potential for serious development in the future.

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