

18.5: Reading- Franchising

Franchising

If you want to be a small business owner but are averse to the risks of starting your own business, you might opt to buy a franchise.

Under this setup, a franchiser (the company that sells the franchise) grants the franchisee (the buyer—you) the right to use a brand name and to sell its goods or services. Franchises market products in a variety of industries, including food, retail, hotels, travel, real estate, business services, cleaning services, and even weight-loss centers and wedding services. There are thousands of franchises, many of which are quite familiar—SUBWAY, McDonald's, 7-Eleven, Holiday Inn, Budget Car Rental, RadioShack, and Jiffy Lube.

As you can see from the figure “The Growth of Franchising, 1980–2007” below, franchising has become an extremely popular way to do business. A new franchise outlet opens once every eight minutes in the United States, where one in ten businesses is now a franchise. Franchises employ eight million people (13 percent of the workforce) and account for 17 percent of all sales in this country (\$1.3 trillion) (“Census Bureau’s First Release of Comprehensive Franchise Data Shows Franchises Make Up More Than 10 Percent of Employer Businesses,” U.S. Census Bureau, September 14, 2010,” U.S. Census Bureau, www.census.gov/newsroom/releases/archives/economic_census/cb10-141.html, accessed August 31, 2011).

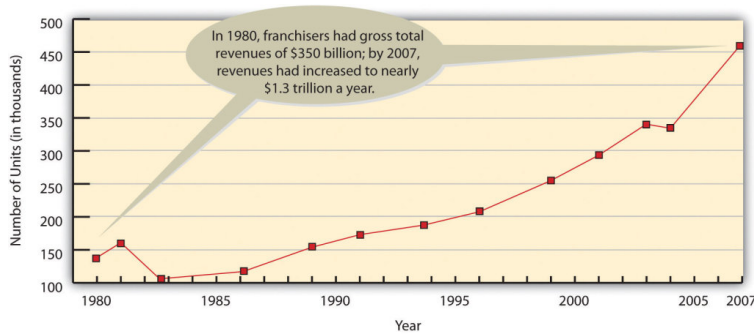


Figure 18.5.1: The Growth of Franchising, 1980–2007

In addition to the right to use a company’s brand name and sell its products, the franchisee gets help in picking a location, starting and operating the business, and advertising. In effect, you’ve bought a prepackaged, ready-to-go business that’s proven successful elsewhere. You also get ongoing support from the franchiser, which has a vested interest in your success.

Not surprisingly, these advantages don’t come cheaply. Franchises can be very expensive, usually depending on the amount of business that a franchisee is expected to do. KFC franchises, for example, require a total investment of \$1.3 million to \$2.5 million each. This fee includes the cost of the property, equipment, training, start-up costs, and the franchise fee—a one-time charge for the right to operate as a KFC outlet. McDonald’s is in the same price range (\$1.1 million to \$1.9 million). SUBWAY sandwich shops are more affordable, with expected total investment ranging from \$84,000 to \$258,000. If you’d prefer teaching dance and exercise classes, you could get a Jazzercise franchise for anywhere from \$3,000 to \$76,000. If you don’t want to deal in food or dance, you might want to buy a dating service. The Right One® franchises go for an initial investment of \$98,000 to \$254,000, depending on location.

In addition to your initial investment, you’ll have to pay two other fees on a monthly basis—a royalty fee (typically from 3 to 12 percent of sales) for continued support from the franchiser and the right to keep using the company’s trade name, plus an advertising fee to cover your share of national and regional advertising. You’ll also be expected to buy your products from the franchiser.

Why do would-be business owners like franchises? For one thing, buying a franchise lets you start up under fairly safe conditions, with a proven model for running a company and a permanent support team. You can profit from name recognition without having to develop your own image in the marketplace, and you can be your own boss (as long as you comply with the standards set by the franchiser).

But there are disadvantages. The cost of obtaining and running a franchise can be high, and you have to play by the franchiser’s rules, even when you disagree with them. The franchiser maintains a great deal of control over its franchisees. For example, if you own a fast-food franchise, the franchise agreement will likely dictate the food and beverages you can sell; the methods used to

store, prepare, and serve the food; and the prices you'll charge. In addition, the agreement will dictate what the premises will look like and how they'll be maintained.

Finally, franchisers don't always keep their promises. What do you do if the promised advertising or employee training doesn't materialize? What do you do if you're forced to make unnecessary and costly alterations to your premises, or the franchising company sets up a competing establishment nearby? What if the franchising company gets bad press, which, in turn, hurts your sales? You always have the option of suing the franchiser, but this is time-consuming and costly. As with any business venture, you need to do your homework before investing in a franchise.

Check Your Understanding

Answer the question(s) below to see how well you understand the topics covered in this section. This short quiz does **not** count toward your grade in the class, and you can retake it an unlimited number of times.

Use this quiz to check your understanding and decide whether to (1) study the previous section further or (2) move on to the next section.

<https://assessments.lumenlearning.com/assessments/188>

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