THE ROLE OF HOST COUNTRY CHARACTERISTICS AND THE FRANCHISOR PROFILE IN THE CHOICE OF FOREIGN ENTRY MODE IN INTERNATIONAL FRANCHISING

ABSTRACT

Franchisors have many options when seeking to expand their business into foreign countries. Specifically, they can enter new markets in one of four ways: i) direct franchising; ii) master franchising; iii) joint venture; or iv) direct investment. The scant theoretical and empirical attention given to this topic has usually been examined from a U.S. and British base, which in most cases focuses on manufacturing or retailing sectors. To shed light on this issue, this study draws from the Spanish franchise system, -which occupies the third position in Europe in terms of the number of franchisors and the second position related to the quantity of franchisee outlets-, to identify the driving variables that impinge upon a firm's choice of franchising entry mode. In order to advance our understanding and contribute to the literature, this study does not focus simply on one sector of activity, as previous studies in this area. In contrast, the present paper considers all sectors of activity (retailing, leisure, hospitality, consulting, etc.) where the Spanish franchise system is operating. Specifically, in early 2011 Spanish franchise chains have presence in 112 foreign countries through 210 franchisors, with a total of 10,135 outlets established abroad. The sample of this study represents 25% of the entries over a total of 10,135 outlets. Our results show the importance of a number of franchisor characteristics (international experience, brand awareness, and industry type (product versus service), in conjunction with a wide list of host country features (geographical distance, uncertainty avoidance, masculinity, political stability, economic development, unemployment rate and efficiency of contract enforcement), all of which have a driving influence upon the decision of entry mode in international franchising. In sum, this work provides readers with an overview of the current state of international franchising and the foreign entry mode, and proves that foreign entry mode choice in international franchising depends on various franchise chain's characteristics and host country's features that franchisors may evaluate before expanding their businesses abroad. We also expect this work may offer guidance to managers when selecting the best mode of entry in their international franchising

KEYWORDS

Franchising, Foreign Entry Mode Choice, International Marketing.

INTRODUCTION

The expansion of companies overseas has long been an important issue to business researchers, specifically, the preferred mode of entry into foreign countries (Mitra and Golder, 2002; Moore, Doherty and Doyle, 2010; Baena, 2011). Entry mode strategy is defined as “an institutional arrangement that makes possible the entry of a firm’s products, technology, human skills, management, or other resources into a foreign country” (Root, 1987, p. 5). Subsequent definitions were developed around this concept. For instance, Gatignon and Anderson (1988) referred to entry mode as a governance structure that allows a firm to exercise control over its foreign operations. More recently, Sharma and Erramilli (2004) explained entry mode as a structural arrangement allowing a firm to implement its product market strategy in a host country either by carrying out only the marketing operations (i.e., via export modes), or both production and marketing operations (direct investment), whether on its own or in partnership with others (contractual modes vs. joint ventures operations). This choice influences a firm’s resource commitment, investment risk, degree of control, and share of profits (Chang and Rosenzweig, 2001; Shrader, 2001; Herrmann and Datta, 2002; Blomstermo, Sharma and Sallis, 2005; Alon, 2006a; Chiao, Meyer et al., 2009; Chiao, Lo and Yu, 2010).

Regarding the non-equity modes of entry, franchising is an organizational model by means of which local entrepreneurs (termed franchisees) are granted the right to operate one or multiple units of the chain at a location while investing their own funds (Michael, 2003). In return, the franchisee pays the franchisor a royalty based on gross sales. Profits after expenses -including royalties- are received by the franchisee as compensation (Elango, 2007). The literature on franchising has fully covered the key issues in this field, for example: i) the reasons for firms organizing as franchise chains and engaging franchisees (see, e.g., Lafontaine and Kaufmann, 1994; Alon, 2005); ii) franchising efficiency (Lafontaine, 1992); and iii) the relationship between franchisor and franchisee (Sanders, 2002). In contrast, although recently there has been greater effort to examine the scope of franchising from an international standpoint, this aspect has generally received limited academic attention (Contractor and Kundu, 1998a, 1998b; Quinn and Doherty, 2000; Doherty, 2007; Alon, 2010), and little is known about the four modes of entry franchisors can adopt:

1. Direct franchising: This refers to selling the business on an individual basis to buyers (i.e. franchisees) in the host country. This mode of entry offers several advantages for the international franchisor, as fewer financial resources are required and business risks are reduced. However, the franchise chain may also encounter certain difficulties understanding local regulations, languages, business norms, or protecting its intellectual property with unreliable standards of policing and enforcement.

2. Master franchising. This relies on a contractual agreement between the franchisor and an intermediary, who purchases from the franchisor entrant the right to develop its own network of outlets in the host market (thereby becoming the master). This contract gives the franchisor's permission to the master to sub-franchise and sell the format on to independent sub-franchisees. (Alon, 2006a).

3. Establishing a joint venture with a local partner. This mode of entry minimizes country risk and provides access to resources held by local firms, but also entails sharing control and ownership (Meyer et al., 2009). Nevertheless, thorny issues may arise with joint ventures, such as managing a partner whose interests could diverge over time (Chang and Rosenzweig, 2001).

4. Direct investment. This implies setting up a new establishment from scratch or the purchase of a local firm. This mode of entry is typically more susceptible to environmental uncertainty and implies greater exposure to political and economic risk (Herrmann and Datta, 2002).

In sum, the four modes of entry imply different levels of ownership and control, as depicted in Figure 1.

PUT IN FIGURE 1

To date, very few studies have focused on driving factors in the choice of foreign entry mode in international franchising (Contractor and Kundu, 1998a; Alon, 2006b; Park and Sternquist, 2008; Baena, 2009; Moore, Doherty and Doyle, 2010). More importantly, most entry mode literature falls on a single uni-dimensional scale (e.g. joint venture versus wholly owned subsidiaries or direct franchising versus master franchise). Clearly, research is still needed in this area. As an attempt to shed light on this issue, this study considers the whole scenario of entry modes that franchisors may implement in their expansion overseas. Hence, a double set of variables is proposed, including franchisor variables (international experience and brand awareness), as well as various features of the host country (cultural and geographical distance, uncertainty avoidance, masculinity, and economic development). These are the strongest factors influencing the entry mode decision of franchisers when opting for either direct franchising, master franchising, joint venture or direct investment into foreign markets. Additionally, several host country variables were controlled for, such as corruption, political stability, unemployment rates, efficiency of contract enforcement, and industry type (product versus service).

Indeed, the scant theoretical and empirical attention given to this topic has usually been examined from a U.S. and British base, which in most cases focuses on manufacturing or retailing sectors (Alon and McKee, 1999; Doherty, 2007; Elango, 2007; Moore, Doherty and Doyle, 2010). As a result, there is a great need for a deeper exploratory model of international diffusion via franchising, one that can explore this issue by focusing on franchising systems other than those from the U.S. and British models, and consider all sectors of activity (retailing, leisure, hospitality, consulting, etc.). In order to advance our understanding and contribute to the literature, this study does not focus simply on one sector of activity, as previous studies in this area. In contrast, the entire Spanish franchise system has been considered which, occupies the third position in Europe in terms of the number of franchisors (1,069) behind Turkey (1,843) and France (1,569) and the second position related to the quantity of franchisee outlets (64,822), only after Germany (66,400). Moreover, in early 2011 Spanish franchise chains have presence in 112 foreign countries through 210 franchisors, with a total of 10,135 outlets established abroad.

The remainder of this work is structured as follows: The second section provides the conceptual model and hypotheses. Following this, the empirical analysis and results are discussed. Lastly, we describe the implications of these findings for practitioners and researchers, while pointing out the main limitations of the study and recommending avenues for further research.

1. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Among the multiple approaches to this issue, transaction cost analysis (TCA) is the theory most commonly used to explain the entry mode choice phenomenon (Chen and Hu, 2002; Sharma and Erramilli, 2004; Hennart, 2010: Morschett, Swoboda and Scharmm-Klein, 2010). Specifically, TCA posits that firms choose to internalize or externalize exchange relationships based primarily on costs incurred in the exchange process (Liang, Musteen and Datta, 2009). In this sense, franchising is considered a hybrid organizational form, located somewhere between the extremes of vertical integration on the one hand, and completely independent operations on the other. Therefore, a different set of interdependent transaction costs associated with franchising out into host markets can be envisaged:

a) Uncertainty about the future state of the environment coupled with limited ability of decision makers to process information;

b) Bounded rationality. This refers to individuals' rationality being limited by the information they have, their cognitive limitations, and the finite amount of time they have to make decisions; and

c) A small number of buyers or suppliers prone to opportunistic behavior.

All these circumstances give rise to transaction costs (Zou, Taylor and Cavusgil, 2005; Hennart, 2010). Consequently, as stated in Williamson (1975), an interdependent set of transaction costs associated with franchising out into host markets can be envisaged: i) monitoring costs; ii) researching costs from identifying and evaluating potential franchise buyers in the target market; iii) property rights protection costs from preventing contracted parties from operating a similar business in a given territory and/or time once the agreement finishes; and iv) servicing costs from transferring the franchisor's technology and know-how to franchisees.

In this study we present a framework based on TCA that allows one to infer the variables constraining foreign entry mode choice in international franchising, using a franchisor and host country level perspective.

International Experience

Franchise chains interested in expanding beyond the domestic market must develop skills to detect and mitigate potential opportunistic behavior on the part of the franchisee (Elango, 2007). - In fact, greater franchising experience can help the franchisor to select suitable agents (Quinn and Doherty, 2000), by enabling him/her to identify ideal franchisees and rule out requests from interested parties unfamiliar with the local market or its business uses (Elango, 2007). This lessens adverse selection (Sashi and Karuppur, 2002), and makes entering via direct franchising less risky (Dow and Larimo, 2009).

In other words, by applying the work of Eroglu (1992), Shane (1996) and Contractor and Kundu (1998a, 1998b), as well as more recent studies (Sashi and Karuppur, 2002; Park and Sternquist, 2008; Dow and Larimo, 2009; Chiao, Lo and Yu, 2010), we can argue that through experience, the chain slowly accumulates specific and valuable know-how. This improves the use of mechanisms for control, monitoring, and market analysis, which reduces the cost of researching and evaluating potential candidates to be franchisees, thus increasing the likelihood of entering via direct franchising.

Franchise chains with high international experience either do not require the help of a local agent, or they need less of such help (Agarwal and Ramaswami, 1992), as they have enough knowledge of how to do business abroad. As a result, internationally experienced franchisors will avoid collaborative agreements with local agents - master franchisee or joint venture – as these modes of entry entail sharing the profits with the business partners (Chiao, Lo and Yu, 2010); instead, direct investment will be favored. Hence, we make the following propositions:

H1$_a$: The expansion of franchisors with strong international experience is positively associated with direct franchising as entry mode.

H1$_b$: The expansion of franchisors with strong international experience is negatively associated with master franchising as entry mode.

H1$_c$: The expansion of franchisors with strong international experience is negatively associated with joint venture as entry mode.

H1$_d$: The expansion of franchisors with strong international experience is positively associated with direct investment as entry mode.

Brand Awareness

Brand awareness is one of a firm's strongest assets (Voss and Tansuhaj, 1999). Therefore, firms with strong brands tend to control all operations closely in order to prevent problems that could damage their brand (Park and Sternquist, 2008). Specifically, these companies are reluctant to adopt business styles that do not permit strict control over all the production processes, thus discouraging any type of alliance with local partners (Quinn and Doherty, 2000; Sashi and Karuppur, 2002; Garg and Rasheed, 2006). A well-known example is that of Burger King and McDonalds, franchisors which in recent years have repurchased many of their fast-food restaurants in several countries in order to control their operations further. Also, both Coca Cola and Pepsi have bought back many franchisees in Europe, among other markets.

As discussed at the beginning of this study, franchising offers a business formula in which the franchisor provides the franchisee all the necessary knowledge to start the business in a way similar to the rest of the network's members. This system also gives franchisees use of the brand name throughout the life of the franchise contract. Nonetheless, in this relationship the franchisee may feel tempted to act opportunistically and reduce those costs not directly controlled by the franchisor, e.g., quality control, maintenance, etc. In that case, the goal would be to increase profits in the franchisee's short term, with no concern for how this could impact the quality of the product or service, the franchisor's brand, or even the entire franchise network operating under the same brand (Quinn and Doherty, 2000; Sashi and Karuppur, 2002; Garg and Rasheed, 2006). To deal with this problem, franchisors are forced to incur high monitoring cost over their franchisees' activities. Franchise chains have also to be able to specify those "cheating" issues in the franchise contract as contingencies that may negatively impact the business relationship (under conditions of bounded rationality), thus increasing transaction costs (Hennart, 2010).

Based on the previous arguments, we argue that franchisors with high brand awareness will opt for supervising as much as possible all the chain's activities in order to reduce opportunistic behavior from the franchisee partners (direct franchisees or master franchisees). This encourages vertical integration and therefore, the probability of entering via joint ventures or direct investment. Hence, we propose the following:

H2$_a$: The expansion of franchisors with high brand awareness is negatively associated with direct franchising as entry mode.

H2$_b$: The expansion of franchisors with high brand awareness is negatively associated with master franchising as entry mode.

H2$_c$: The expansion of franchisors with high brand awareness is positively associated with joint venture as entry mode.

H2$_d$: The expansion of franchisors with high brand awareness is positively associated with direct investment as entry mode.

Geographic and Cultural Distance

When researchers look at modes of entry, both geographic and cultural distances are of immediate concern, therefore becoming a common focus in much of the literature. Both negatively affect the franchisor's desired level of internationalization (Alon, 2006b). Specifically, there are higher transaction costs associated with managing remote locations, as geographic distance generates costs related to communications, which hinders internationalization (Chen et al., 2009). Geographic distance also raises the level of uncertainty by increasing the information gap between the franchisor and the franchisee and therefore, the costs of monitoring and gathering information (Alon, 2006b).

Similarly, selection and supervision costs are higher in culturally distant markets, as the information asymmetries and the likelihood of opportunistic behavior increases. In this sense, Kogut and Singh (1988) found that when cultural distance is great, companies are more likely to prefer joint ventures to wholly owned operations. Also, the use of master franchising is more likely when the cultural distance is high, as more help is needed from local contacts, the information gathering costs are higher, the potential for cultural misunderstandings is greater, and the possibility of adverse selection problems increases (Contractor and Kundu, 1998b; Alon, 2006). All these issues increase transaction costs (Welsh, Alon and Falbe, 2006; Demirbag, Tatoglu and Glaister, 2009).

In sum, both geographic and cultural distances between the host and home country induce foreign enterprises to seek local support in order to facilitate product adaptation (Chen et al., 2009). They also deter full resource commitment (direct investment) and prompt shared equity and control entry modes such as joint ventures (Herrman and Datta, 2002, Chen et al., 2009). Furthermore, franchise chains are likely to obtain perfect (or less flawed) information when they negotiate with only one physical person or legal entity (master franchising), as compared to negotiation processes conducted directly with several geographically and culturally distant agents (direct franchising) (Alon and McKee, 1999; Garg and Rasheed, 2006). Thus, we make the following propositions:

$H3_a$: Expansion of franchising across countries with high geographic distance is negatively associated with direct franchising as entry mode.

$H3_b$: Expansion of franchising across countries with high geographic distance is positively associated with master franchising as entry mode.

$H3_c$: Expansion of franchising across countries with high geographic distance is positively associated with joint venture as entry mode.

$H3_d$: Expansion of franchising across countries with high geographic distance is negatively associated with direct investment as entry mode.

$H4_a$: Expansion of franchising across countries with high cultural distance is negatively associated with direct franchising as entry mode.

$H4_b$: Expansion of franchising across countries with high cultural distance is positively associated with master franchising as entry mode.

H4$_c$: Expansion of franchising across countries with high cultural distance is positively associated with joint venture as entry mode.

H4$_d$: Expansion of franchising across countries with high cultural distance is negatively associated with direct investment as entry mode.

Hofstede's research (1991) revealed that cultures differ on four different dimensions: 1) tolerance for ambiguity or uncertainty avoidance; 2) power distance; 3) individualism/collectivism; and finally 4) masculinity. In 2001, this author added a new measure, *long-term orientation*. All of these dimensions have been calculated for different countries and have been highly cited in the literature (see, e.g., Mitra and Golder, 2002; Demirbag, Tatoglu and Glaister, 2009).

Literature has suggested, however, that foreign entry mode choice may be constrained by only some of the four cultural dimensions used to calculate Hofstede's cultural distance (Hoffman and Preble, 2001). In particular, as argued in Baena's study (2009), entrepreneurs from cultures with high uncertainty avoidance (low tolerance for ambiguity) may be more likely to adopt franchising as a business format because of their willingness to enter into a calculated risk situation. Franchising can be seen as a method of economic development that reduces entrepreneurial risk by transferring a proven retail concept to franchisees (Michael, 2003). Following this reasoning, the number of agents aspiring to be franchisees (direct or master) increases, which fosters the international expansion of the franchise chain. Moreover, as the number of candidates increases, the risk of selecting the wrong sort of franchisee (one who might engage in opportunistic behavior contrary to the franchisor's interests) decreases, therefore reducing the market research cost of identifying and evaluating potential franchise buyers in the target market.

As stated in Alon (2006b), a host country's masculinity may determine entry mode choice in international franchising. Cultures that favor competition (high masculinity) tend to reward entrepreneurship (Hoffman and Preble, 2001). This characteristic reduces the number of candidates interested in being franchisees, since they are adverse to following the franchisor's rules. Because of this, finding adequate franchisees in the target market (direct or master franchisees) will require more researching, data gathering, and cost evaluation. Thus, in host countries with high masculinity, franchisors will favor entry via joint ventures and direct investment. Based on the above, we propose the following:

H5$_a$: Expansion of franchising across countries with high uncertainty avoidance is positively associated with direct franchising as entry mode.

H5$_b$: Expansion of franchising across countries with high uncertainty avoidance is positively associated with master franchising as entry mode.

H5$_c$: Expansion of franchising across countries with high uncertainty avoidance is negatively associated with joint venture as entry mode.

H5$_d$: Expansion of franchising across countries with high uncertainty avoidance is negatively associated with direct investment as entry mode.

H6$_a$: Expansion of franchising across countries with high masculinity is negatively associated with direct franchising as entry mode.

H6$_b$: Expansion of franchising across countries with high masculinity is negatively associated with master franchising as entry mode.

H6$_c$: Expansion of franchising across countries with high masculinity is positively associated with joint venture as entry mode.

H6$_d$: Expansion of franchising across countries with high masculinity is positively associated with direct investment as entry mode.

Economic Development

The need to systematically evaluate and select foreign markets based on their economic development has been stressed by many researchers, as this choice is critical for a business's future success (Rahman, 2006). Given that franchising is dominated by services or products associated with branding and services, investing in a viable host economy where people are able to afford them (rather than perform them themselves) is crucial to the growth of business activity via franchising (Alon and McKee, 1999; Alon, 2006a; Baena, 2009). Thus, as economies become more affluent, there is a greater shift to services which, as shown by Hoffman and Preble (2001), provide more opportunities for firms to expand.

A country's stronger economic development is associated with business growth (Alon, 2010), and intellectual property rights protections (Contractor and Kundu, 1998b). All these issues reduce the adverse selection problem and the costs related to monitoring the franchisee's behavior. This leads us to hypothesize that franchise chains would support franchising as entry mode in foreign markets with strong economic development. Nonetheless, as those nations also have less exposure to economic and business risks (Herrmann and Datta, 2002), franchisors willing to enter them do not need alliances with local partners (as direct franchisees or master franchisees), or they need less of such help. This gives the franchise chain the chance to create an entirely new organization that meets its own requirements (joint venture or direct investment) and to avoid any profit sharing with franchisees. Based on this discussion, we propose the following:

H7$_a$: Expansion of franchising across countries with strong economic development is negatively associated with the propensity for direct franchising.

H7$_b$: Expansion of franchising across countries with strong economic development is negatively associated with the propensity for master franchising.

H7$_c$: Expansion of franchising across countries with strong economic development is positively associated with the propensity for joint venture.

H7$_d$: Expansion of franchising across countries with strong economic development is positively associated with the propensity for direct investment.

METHODOLOGY

Population, Sample, and Data Collection

With regard to the population of this study, data on market entries were obtained from the Spanish franchise system, which occupies the third position in Europe in terms of the number of franchisors (1,019) and the second position related to the quantity of franchisee outlets (65,026). As of early 2011, Spanish franchisors are present in a total of 112 foreign countries through 210 chains, with a total of 10,135 outlets established abroad. Data were obtained by contacting the Spanish Franchise Association and the leading Spanish franchising Consultant Group, Tormo & Asociados. We also considered various studies published in the business press, as well as web pages of the main Spanish franchise chains and the most important international franchising associations (*International Franchise Association, Global Franchise Network,* etc). We finally obtained data on the entry modes adopted by 43 Spanish chains in 2,532 outlets across 62 foreign nations.

Thus, the sample of this study represents 25% of the entries effected by Spanish franchisors overseas (a total of 10,135). It is important to point out that databases created with information from secondary sources have been used previously in studies on franchising (Alon, 2001; Baena, 2009). Even though the collected data are provided by franchisors, the literature demonstrates that annual reports validate more than 80% of this. Therefore, no significant bias appears to exist in this sample (Shane, 1996).

As shown in Figure 2, Spanish franchisors tend to use direct franchising and master franchising to enter foreign markets. Jointly, they represent nearly 80% of all the entry modes computed in this study (2,532). On the contrary, joint ventures (6.28%) and direct investment (17.65%) are much less preferred by Spanish franchisors for entering countries. Data also reveal the relevant international spread of Spanish chains in many business sectors. This international diffusion is particularly intense in the fashion, retail and hotel and restaurant sectors. As depicted in Figures 3 and 4, companies like Mango, Zara, Stradivarius, Bershka, Massimo Dutti, Springfield, Oysho, Adolfo Dominguez, Pull and Bear, and Paellador are among the 20 Spanish franchise chains with highest international diffusion in 2011, both in terms of countries and outlets operating abroad.

PUT IN FIGURE 2

PUT IN FIGURES 3 AND 4

Dependent Variable

The foreign entry mode choice of Spanish franchisors was assessed using four dependent variables as follows:

i. DIRECT FRANCHISING (DIRECTF) measures the total number of outlets established via direct franchising by each franchisor in each of the foreign nations of operation.

ii. MASTER FRANCHISING (MASTERF) measures the total number of outlets established via master franchising by each franchisor in each of the foreign nations of operation.

iii. JOINT VENTURE (JOINTV) measures the total number of outlets established via joint venture by each franchisor in each of the foreign nations of operation.

iv. DIRECT INVESTMENT (DIRECTINV) measures the total number of outlets established via direct investment (franchisor company owns 100 per cent of the franchisee outlet) by each franchisor in each of the foreign nations of operation.

Independent Variables

The international experience of franchisor companies is usually defined as the geographical spread of franchising within a foreign country (Hoffman and Preble, 2001). It is then assessed by computing the number of outlets each franchisor company has abroad (OUTLETS). In our data set, this variable ranged from 2 (Cebado, a hairdressing chain) to 1,239 outlets (Mango, a fashion retail chain) overseas. However, this measurement has one weakness in that it may not reveal the real degree of international expansion. As previously shown in Figures 3 and 4, the Spanish chains with the greatest number outlets abroad are not always the same ones that are operating in the most countries. In order to deal with this problem, we followed Baena's (2011) study and a second variable was established to measure international experience, defined as the number of foreign countries (COUNTRIES) in which each franchisor is doing business. In our data set, this variable ranges from 2 countries (in the case of Cebado) to 100 (Mango).

Brand awareness of Spanish franchisors with presence abroad (BRAND) is computed by using data from the las study conducted by the Forum of Leading Spanish Brands (Foro de Marcas Renombradas Españolas (FMRE), www.brandsofspain.com). According to the technical specifics of this report, the Forum used a sample of 4,800 people to assess the brand awareness of 118 different product categories, including most of the major Spanish franchise brands. The paper has its theoretical grounding in the concepts of typicality and dominance developed by Simonson (1993) and Peterson, Smith and Zerrillo (1999). These researchers established two fundamental concepts for assessing and stimulating a brand's recognizability (using the concepts of fame, prestige and recognizability synonymously): typicality[1] and dominance[2]. Peterson, Smith and Zerrillo (1999) applied the concepts of typicality and dominance to assess the public awareness of 28 brands, using a survey of 464 participants. The FMRE used the same method, finally calculating brand awareness and recognizability as the average of typicality and brand dominance.

In dealing with geographical distance (GEODIST), sometimes we were not able to know the exact physical location of all the outlets considered in this work. As a solution for this, this variable was drawn from the kilometer distance between the capital of the franchisor's home country (Madrid, by default) and the capital of the nation where the outlet is located, as done in previous literature (Baena, 2009; Alon, 2010). In our sample, this variable ranges from 492 (Portugal) to 11,381 (Singapore).

Cultural distance (CULTDIST) was assessed by using Hofstede's (2001) work. Following Kogut and Singh (1988), a cultural index was created as follows:

$$\text{CULTDIST} = \frac{\frac{(I_{hi} - I_{hj})^2}{V_h}}{4}$$

Whereby I_h, with h = 1, 2, 3, and 4, referring to each of the four cultural factors identified by Hofstede (2001). V_h represents the variance of each factor. Accordingly, for each of the four cultural factors, the national value was subtracted from the value of Spain, squared, and subsequently divided by the standard deviation of this metric. In our data set, the cultural distance index varies from 0 (for Spain, by default) to 13.32 (Singapore). Data on uncertainty avoidance (UNCERAV) and masculinity (MASCULIN) were also obtained from Hofstede's work (2001). These variables are staples of international management and marketing literature, having been used in many published studies (Michael, 2003). Moreover, as previous literature discussed, the results have been found to be both valid and reliable (Sakarya, Eckman and Hyllegard, 2007; Yamin and Golesorkhi, 2010).

Lastly, the level of economic development (ECODEV) was computed by using the gross domestic product per capita as a proxy variable, as suggested in recent studies (Alexander, Rhodes and Myers, 2006; Sakarya, Eckman and Hyllegard, 2007; Alon, 2010). Data for this variable were collected from the World Bank Report published in 2010. In the data set, it ranks from 2.77 (Moldova) to 78.72 (Luxembourg).

Control Variables

As stated in the Introduction, this paper controls for a host country's political stability, unemployment rate, transparency and efficiency of contract enforcement in conjunction with the chain's industry type (product versus service).

The level of political stability (POLITICAL) was assessed using the 2010 International Monetary Fund (IMF) Report. Lowest values correspond to nations showing high political stability and vice versa (in the data set 0.2 corresponds to Norway). The World Bank Annual Report 2010 was used to measure the unemployment rate (UNEMPLOY), as in previous literature (Habib and Zurawicki, 2002; Baena, 2009). The host country's level of corruption (TRANSPAR) was computed by using the 2010 Transparency International Index. Highest values correspond to nations showing high transparency. In the data set, corruption levels range from 1.9 (Angola and Venezuela) to 9.3 (Denmark).

Another control variable is that of efficiency of contract enforcement, which this study assessed by following the evolution of a disputed sale of goods, tracking the time, cost, and number of procedures involved from the moment the plaintiff files the lawsuit until actual payment. As suggested in Djankov et al., (2003), this work uses the three indicators developed by the *Doing Business Index* published in 2010 by the World Bank Group:

- Number of procedures from the moment the plaintiff files a lawsuit in court until the moment of payment (PROCED);
- Time elapsed (calendar days) in resolving the dispute (DURATION); and
- Cost in court fees and attorney fees, where the use of attorneys is mandatory or common, expressed as a percentage of the debt value (COST).

Finally, a franchise chain's industry type (ACTIVITY) was measured with a binary variable that takes a value of 0 when it is product based, and 1 when the business is service based. This relied on a classification compiled by the franchising consulting firm, Tormo & Asociados.

2. RESULTS

The descriptive statistics and the correlation matrix are reported in Tables 1 and 2.

PUT IN TABLES 1 AND 2

Analysis of the proposed hypotheses was conducted by computing OLS regression analyses. The variables that did not follow a normal distribution were entered into the model in logarithmic form. Also, the dependent variables (DIRECTFR, MASTERF, JOINTV, and DIRECTINV) were standardized. To test the existence of collinearity among the variables, the Variance Inflation Factor (VIF) and Tolerance were computed. None was statistically significant, suggesting that collinearity was not a problem in our regression models. For additional confirmation of these results, we calculated the determinant of the correlation matrix, finding a value of 1, and were thus able to rule out problems of multicollinearity. Results are shown in Table 3.

PUT IN TABLE 3

As shown, franchise chains with international experience (OUTLETS and COUNTRIES) will opt for direct franchising to enter markets characterized by high uncertainty avoidance (UNCERAV) but low masculinity (MASCULIN) and geographic distance (GEODIST). Consequently, results support hypothesis H5a at the 0.05 level, as well as hypotheses H1a, H3a and H6a at the 0.1 level. In contrast, franchisors prefer to enter foreign markets via master franchising if host country corruption (TRANSPAR) and political instability (POLITICAL) are high.

Alternatively, franchisors achieve entry through joint ventures if they are service business (ACTIVITY) and lack international experience (COUNTRIES and OUTLETS). Moreover, franchisors with high brand awareness (BRAND) adopt this mode to enter nations characterized by high political stability (POLITICAL), geographic distance (GEODIST), and efficiency of contract enforcement (PROCED and COST) but low unemployment rates (UNEMPLOY). Therefore, hypotheses H1c and H2c were supported at the 0.05 level and hypothesis H3c, at the 0.1 level.

Finally, direct investment is preferred by those chains with high international experience (COUNTRIES), and brand awareness (BRAND) that enter foreign markets characterized by low geographic distance (GEODIST), uncertainty avoidance (UNCERAV) and corruption (TRANSPAR), but high levels of masculinity (MASCULIN), economic development (ECODEV), and efficiency of contract enforcement (DURATION). This supports hypotheses H1d and H6d at the 0.05 level, and hypotheses H2d, H3d, H5d, and H7d at the 0.1 level.

DISCUSSION AND CONCLUSION

International franchising has shown exponential growth over the last two decades, both in the United States and beyond (Alon, 2001). This growth has been fueled by both push factors, such as saturation, competition plus diminishing profits in the domestic markets, and pull factors, e.g., the new free markets of the Eastern bloc countries and the emergence of some newly industrialized countries into the international marketplace (Alon and McKee, 1999; Hoffman and Preble, 2001). Nevertheless, despite more attempts in recent years to examine the scope of franchising from an international standpoint, the academic attention given to this topic is very limited (Quinn and Doherty, 2000; Doherty, 2007; Alon, 2010) and dominated by studies from U.S. or British perspectives (Alon and McKee, 1999; Doherty, 2007; Elango, 2007; Moore, Doherty and Doyle, 2010). In an attempt to shed light on this topic, this paper analyzes the entry mode choice followed by Spanish franchisors across foreign nations.

The results confirm arguments that firms possessing significant brand awareness will prefer entry modes that allow them to control business operations (i.e., joint venture and direct investment), since a firm’s brand is particularly susceptible to franchisee opportunism (Contractor and Kundu, 1998b; Park and Sternquist, 2008). For instance, this is the case of

Zara (retail fashion chain), whose international strategy is mainly company-owned franchising. In fact, the company entered Russia and Finland via franchising with the agreement that they could reacquire these stores when resources became available. Similarly, in 2006, after China changed their joint venture laws, Zara was able to enter this country with their own stores.

A host country's corruption forces franchisors to engage in resource-wasting, profit-seeking activities, further burdening them with the additional costs of enforcing franchise contracts in courts, and the direct cost of bribes. Therefore, transparency is positively associated with entries via direct investment, as argued in previous literature (Rodriguez, Uhlenbruck and Eden, 2005; Teyin-Koru, 2006). Findings also show a positive association between direct investment and a host country's economic development, together with efficient contract enforcement. Indeed, this entry mode allows franchisors to gain information from the market and adapt the business offering to the market's characteristics without having to share profits with any local partner.

It is important to note, however that, most franchisors lack the necessary resources and cannot afford direct investment as foreign entry mode. In fact, it placed second-to-last among the available options for international franchising chosen by Spanish franchisors (17.65%). Thus, once a firm is familiarized with the characteristics of the country targeted for investment, local expansion is usually done via direct franchising, as this mode is faster. This is the case of certain leading Spanish franchisors like Neck and Neck and Mango (retail fashion chains). Results also show direct franchising to be the preferred mode of entry among franchise chains with high international experience when entering markets characterized by uncertainty avoidance but low masculinity and geographical distance. In contrast, franchisors seeking to expand their business across nations with political instability will opt for master franchising. Master franchising is also preferred for entering foreign markets characterized by low transparency (high corruption). This is the case, for instance, of Telepizza (fast food chain), which entered Guatemala by signing an agreement with the master franchisor, Pollo Campero, the largest fast food chain in Latin America.

Joint ventures account for approximately 6.28% of total entries considered in our data base. They are particularly chosen by Spanish franchisors with financial resources but limited market knowledge that are willing to enter geographically distant markets, like China or Japan. After analyzing the data set, we found several cases where entry mode via joint venture is designed as a short-term strategy just to gain market knowledge and access to sociopolitical contacts, and/or to maneuver around legal restrictions (e.g., in some countries, 100% foreign investment is not allowed). For example, Mango (fashion retail chain) entered Japan via joint venture. However, in 2006 the firm bought the shares from its local partner, Mitsui, and therefore, it currently owns 100% of Mango retail stores in that country. Additionally, as joint venture entails sharing control and ownership, allowing firms to reduce the uncertainty exposure of the foreign-going firm (Blomstermo, Sharma and Sallis, 2005; Meyer et al., 2009), this entry mode is preferred by franchisors with brand awareness who are willing to expand their business across nations showing political stability.

Cultural distance has traditionally been identified as a key variable in entry mode decisions of multinational companies (Demirbag, Tatoglu and Glaister, 2009). However, in spite of its negative association with direct franchising and direct investment, and yet positive association with master franchising and joint venture (as predicted in H4a, H4b, H3c and H4d), none of those associations was statistically significant. In contrast, the effect of two cultural dimensions - uncertainty avoidance and masculinity - was statistically significant. Thus, as suggested in previous literature (Hoffman and Preble, 2001; Alon, 2006b; Baena, 2009) the foreign entry mode choice may not be constrained by cultural distance as a whole, but by only some of the cultural dimensions that compound Hofstede's cultural distance. Specifically, the relationship between uncertainty avoidance with direct franchising and direct investment was positively and negatively significant, respectively. This fact allows us to conclude that franchising reduces entrepreneurial risk by transferring management and marketing expertise from the franchisor to the franchisee (Eroglu, 1992; Sashi and Karuppur, 2002; Michael, 2003). In contrast, cultures that favor competition (high masculinity) tend to reward entrepreneurship and thus, there is less likelihood of finding local agents willing to become franchisees. This explains the positive and significant association found between masculinity and direct investment, and the negative relation between entries via direct franchising and host country's masculinity.

This study also tests the effect of the host country's unemployment rate on foreign entry mode choice. The significant association between this variable and entries via joint venture shows that franchising may be considered an alternative to other employment. In particular, as stated in Michael (2003), when wages and other benefits associated with alternative forms of employment fall, the attractiveness of being self-employed in an independent business increases. Namely, franchisors entering countries characterized by high unemployment rate may find many agents willing to spend their savings in order to become franchisees or master franchisees. This reduces the likelihood of entering via equity modes (i.e., joint venture).

Finally, it is worth mentioning that as shown in the obtained findings, entries via joint venture are preferred by service based business franchisors. In this sense, one can argue that the specific features of a product (composition, etc.) can be standardized and therefore, more easily replicated than when dealing with intangible assets, such as those of service based companies (Combs and Ketchen, 1999). Moreover, a chain whose business line is selling products instead of services tends to have more structured control processes and can easily shows the franchisee how to carry out various aspects of the business, while controlling for compliance, managing inventory, etc. As a result, given that service chains need higher franchisee (direct or master franchisee) training and monitoring as compared to product based ones (Mitra and Golder, 2001; Shrader, 2001), the most logical route is to avoid franchising and delegate supervision to a local partner (joint venture), someone who understands the specific characteristics of the host country. Examples of Spanish service chains entering foreign nations via joint venture are Pans & Company (fast food chain) in El Salvador.

Theoretical and Practitioner Implications

This work provides readers with an overview of the current state of international franchising and the foreign entry mode. We hope it serves as a useful starting point for future investigation by researchers interested in this topic.

The obtained results prove that foreign entry mode choice in international franchising depends on various franchise chain's characteristics and host country's features that franchisors may evaluate before expanding their businesses abroad. To shed light on this issue, this study draws from the Spanish franchise system to identify the driving variables that impinge upon a firm's choice of franchising entry mode. It also considers all sectors of activity (retailing, leisure, hospitality, consulting, etc.) to examine the complete set of entry modes that franchisors may implement in their expansion overseas: direct franchising, master franchising, joint venture, and direct investment.

We also believe that our study offers further contributions: Indeed, it empirically demonstrates that Hofstede's conceptualization of culture may not be valid for examining the host market conditions driving entry mode choice in international franchising; additionally, results show the effects of two cultural dimensions (uncertainty avoidance and masculinity) on the entry mode choice, as suggested in previous literature (Hoffman and Preble, 2001; Alon's 2006b; Baena 2009).

Finally, the present paper develops and tests a model that could be useful for managers that consider moving abroad. Specifically, it proves that franchisors should be aware of the chain's characteristics and host country's features found in this study as driving factors of foreign entry mode choice. We thus expect this work may offer guidance to managers when selecting the best mode of entry in their international franchising.

LIMITATIONS AND DIRECTIONS FOR FUTURE RESEARCH

Our results offer several firm conclusions regarding variables that may constrain foreign entry mode choice in international franchising. However, this study has some limitations that need to be addressed. Firstly, this study only refers to Spanish franchise chains. We encourage an analysis of franchisors coming from other nations in order to test whether the results obtained in this study can be generalized to all franchise systems. Secondly, conceptually and empirically more work is necessary to refine the model, identifying the key variables driving the entry mode choice of international franchising. For instance, as stated in this study, no significant association was found between cultural distance and the independent and control variables. This could imply that a new conceptualization of culture, like GLOBE, may be considered (Javidan et al., 2006; Sarala and Vaara, 2010; Stephan and Uhlaner, 2010). Therefore, we propose the study of this issue as further research.

Lastly, this study identifies certain firm and country factors that influence entry mode choice but it does not endeavor to classify the relative importance of these variables. While it was not an objective of this work to find such relative importance (if any), further research may be conducted to assign a numerical weight to each factor as indication of their relative importance in the choice of foreign entry mode.

Overall, more work is necessary in this area, both conceptually and empirically speaking. Indeed, we hope our findings contribute to the development of a robust research agenda.

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Figure 1: Foreign Entry Mode Choice for Franchisor Companies

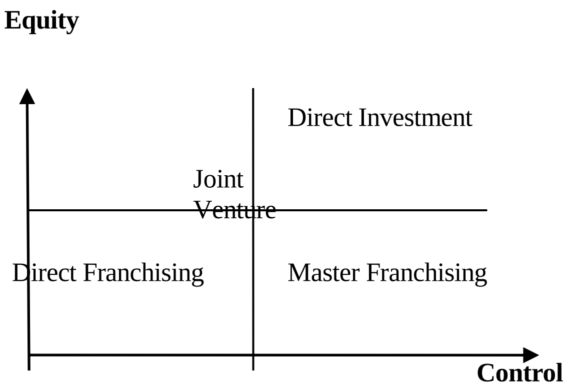
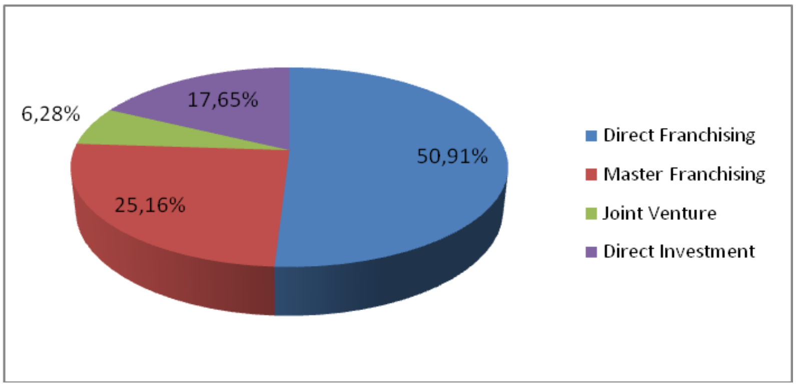


Figure 2: Mode of Entry Adopted by Spanish Franchisors Overseas in 2011



Figures 3 and 4: Top 20 Spanish Franchise Chains with Highest International Diffusion (Outlets and Countries) in 2011.

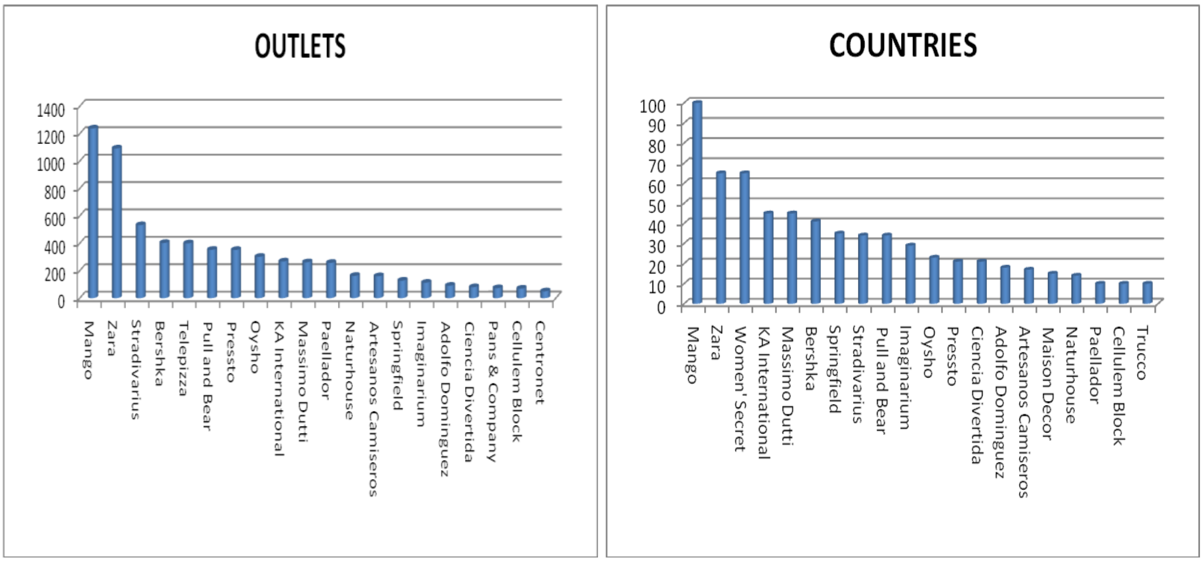


Table 1: Descriptive Statistics

VARIABLES	MINIMUN	MAXIMUN	MEAN	STANDARD DEVIATION
DIRECTF	1.000	91.000	12.047	19.751
MASTERF	1.000	56.000	8.493	10.563
JOINTV	1.000	40.000	7.571	10.567
DIRECTINV	1.000	80.000	11.462	17.313
OUTLETS	2.000	1,239.000	459.299	442.298
COUNTRIES	2.000	100.000	39.932	29.653
ACTIVITY	0.000	1.000	0.359	0.4807
BRAND	1.000	98.200	45.542	34.074
CULTDIST	0.360	13.320	4.099	3.234
GEODIST	492.000	11,381.000	3,586.803	3,257.454
POLITICAL	0.200	6.700	3.397	1.646
TRANSPAR	1.900	9.300	5.634	2.076
ECODEV	2.770	78.720	24.506	13.989
UNEMPLOY	0.000	33.800	8.135	4.284
UNCERAV	8.000	112.000	75.839	23.428
MASCULIN	5.000	95.000	51.972	18.305
PROCED	20.000	50.000	33.765	6.290
DURATION	150.000	1,459.000	611.590	298.206
COST	2.000	52.600	20.267	10.329

Table 2: Correlation Matrix

Variables	directf	masterf	jointv	directinv	outlets	countries	brand	geodist	cultdist	uncerav	masculin	ecodev	political	unemploy	transpar	proced	duration	cost	activity
directf	1.000	-0.692	-0.795	0.678	0.051	0.052	0.221	-0.041	-0.135	0.285	-0.163	-0.027	0.153	0.024	0.035	-0.065	-0.061	-0.172	0.068
masterf		1.000	-0.073	-1.000	-0.005	-0.098	0.062	0.052	0.022	0.238	-0.187	-0.214	0.277	0.034	-0.073	0.000	0.161	0.130	-0.225
jointv			1.000	-0.026	0.246	0.056	0.314	0.112	0.245	-0.210	0.012	-0.014	0.282	0.139	-0.246	0.212	0.279	0.245	-0.044
directinv				1.000	-0.003	-0.211	0.175	-0.007	-0.258	0.228	0.127	0.066	-0.426	-0.341	0.082	-0.001	-0.203	-0.167	0.288
outlets					1.000	0.673	0.586	-0.046	0.081	-0.073	0.058	0.056	-0.134	-0.022	0.054	-0.037	-0.086	0.020	-0.457
countries						1.000	0.565	-0.147	0.120	-0.134	0.101	0.120	-0.205	-0.014	0.142	-0.119	-0.175	-0.037	-0.558
brand							1.000	-0.067	-0.009	0.068	0.026	0.024	-0.073	-0.090	0.049	-0.045	0.027	-0.072	-0.281
geodist								1.000	0.331	-0.184	0.012	-0.346	0.211	-0.013	-0.329	0.116	0.102	0.290	0.307
cultdist									1.000	-0.764	0.057	0.182	-0.411	-0.197	0.418	-0.398	-0.236	0.204	-0.101
uncerav										1.000	-0.052	-0.258	0.353	0.087	-0.369	0.253	0.263	-0.098	0.117
masculin											1.000	-0.049	-0.029	0.099	-0.078	-0.053	0.096	0.020	-0.146
ecodev												1.000	-0.587	-0.295	0.679	-0.377	-0.360	-0.196	-0.252
political													1.000	0.270	-0.717	0.421	0.334	0.211	0.333
unemploy														1.000	-0.312	0.317	0.145	0.191	0.081
transpar															1.000	-0.538	-0.467	-0.243	-0.300
proced																1.000	0.437	-0.061	0.182
duration																	1.000	0.210	0.171
cost																		1.000	0.186
activity																			1.000

Table 3: Regression Analyses

VARIABLES	**REGRESSION COEFFICIENTS**							
CONSTANT	-0.230	25.819	3.151	-0.984	-0.019	-0.057	4.198	0.177
OUTLETS	**0.004 ***	0.040	0.002	0.002	**-0.026 ***	**-0.001 *****	0.004	0.004
COUNTRIES	**0.049 ***	**0.051 ***	-0.026	-0.028	-0.039	**-0.036 ***	0.010	**0.009 *****
BRAND	-0.057	-0.053	-0.022	-0.018	**0.007 *****	**0.003 *****	**0.042 ***	**0.038 ***
GEODIST	**-0.142 ***	-0.009	0.115	-0.012	**0.067 ***	0.000	0.000	**-0.001 ***
CULTDIST	-0.846		0.316		0.006		-0.410	
UNCERAV		**0.143 *****		0.021		-0.010		**-0.008 ***
MASCULIN		**-0.099 ***		0.030		0.009		**0.076 *****
ECODEV	-0.029	-0.063	-0.029	-0.012	0.018	0.036	**0.149 ***	**0.126 ***
POLITICAL	0.387	0.549	**0.346 *****	**0.236 *****	**-0.0178 ***	-0.104	-0.118	-0.172
UNEMPLOY	0.459	0.374	0.170	0.159	**-0.003 ***	-0.001	-0.151	-0.301
TRANSPAREN	0.541	0.132	**-0.27 ***	-0.239	-0.027	0.062	**1.411 *****	1.025
PROCED	-0.169	-0.258	0.001	0.001	**-0.041 ***	0.034	-0.084	-0.032
DURATION	0.000	0.002	0.002	0.001	0.000	-0.003	**-0.007 *******	**-0.022 ***
COST	0.016	0.016	0.064	-0.025	-0.014	**-0.018 ***	0.021	0.001
ACTIVITY	-0.490	-0.365	0.294	0.099	**1.25 *****	**1.385 ***	-0.356	-0.183
	Dependent Variable: Direct Franchise N= 1,289		Dependent Variable: Master Franchise N=637		Dependent Variable: Joint Venture N=447		Dependent Variable: Direct Investment N=159	
	R^2: 0.357 Adj. R^2: 0.205 F =1.763 **p= 0.053**	R^2: 0.399 Adj. R^2: 0.259 F =2.052 **p= 0.017**	R^2: 0.344 Adj. R^2: 0.144 F =1.378 **p= 0.239**	R^2: 0.389 Adj. R^2: 0.147 F =1.269 p= 0.284	R^2: 0.330 Adj. R^2: 0.287 F=1.269 p=0.284	R^2: 0.679 Adj. R^2: 0.487 F = 2.241 p=0.227	R^2: 0.319 Adj. R^2: 0.102 F = 1.371 p= 0.179	R^2: 0.364 Adj. R^2: 0.132 F = 1.656 **p= 0.071**

* Significant at 10% level of significance
** Significant at 5% level of significance
*** Significant at 1% level of significance