

Franchise and Opportunities for Local Food Processing Industry

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Franchise has become increasingly familiar to Vietnamese business circles when consumers may have a cup of Gloria Jean's coffee and Phở 24 in the morning, KFC at noon, and buy some cakes from Kinh Đô Bakery shops in the evening.

The Vietnam's 2005 Commerce Law defines franchise as a commercial activity in which the franchisor allows and requires the franchisee to sell goods or services according to (1) rules and regulations set by the franchisor associated with its brand, trade mark, know-how, slogan, logo and advertisement; and (2) control and support given by the franchisor in running the business.

According to either local or foreign definitions, the franchise is always a way of doing business associated with intellectual property rights that aim at ensuring the reasonable and productive cooperation between the franchisor and franchisee in which the latter has rights to sell or distribute goods or services in certain areas and during a certain period according to plans or marketing campaigns carried out by the franchisor in order to ensure the uniformity of goods and services and avoid bad effects on the franchisor's brand names. In such a contract, the franchisee may pay the franchisor by a royalty on the number of units sold or produced.

1. Franchise in Vietnam today

In the past three years, the franchise business experienced good development when many local companies, such as Phở 24, Kinh Đô Bakery, Nhà Xinh, and Thời Trang Foci, etc. became franchisors while others are building their brand names and preparing to franchise them, such as Nước Mía Siêu Sạch (extremely fresh sugarcane juice) and Passio Coffee. Some Vietnamese franchisors have established footholds in foreign markets: Phở 24 has had its stores in the Philippines, Malaysia, South Korea and Australia; and Trung Nguyên Coffee in Japan, the U.S. and Australia. Number of foreign franchisors with cooperation with local companies is also on the increase. These facts show that the Vietnamese market is attractive in the eyes of foreign franchisors.

The Vietnamese population is over 80 million and 50% of which is under 30 years of age. A survey in 2006 of consumption of high-quality local goods shows that persons from 22-55 years of age are the

highest-spending group (87% of them spend at least VND500,000 a month). High level of literacy also help ad messages reach the public easily. Distribution of townsfolk all over big cities, instead of concentrating in high buildings or apartment blocks, allows development of chain stores in each district because local residents need convenient stores. In addition, home delivery and transport are not well developed, which make them more dependent on stores for their needs.

When their income and living standard are improved, consumers tend to pay more attention to quality of goods and services and brand names than to prices. They are also more affected by advertisement than before and modern ways of shopping (AT Kearney ranks Vietnam the third place in terms of potential for retail market), which also leads to possibility of developing the franchise business.

Other macroeconomic factors affecting the future of this business are steady growth rates in recent years (Vietnam is considered as being in a hot developing period like China in 2003); political stability and favorable business climate.

Local companies, in addition, are active and industrious but they usually lack business experience and managerial skills. Entering franchise contracts could be seen as a measure to deal with these shortcomings.

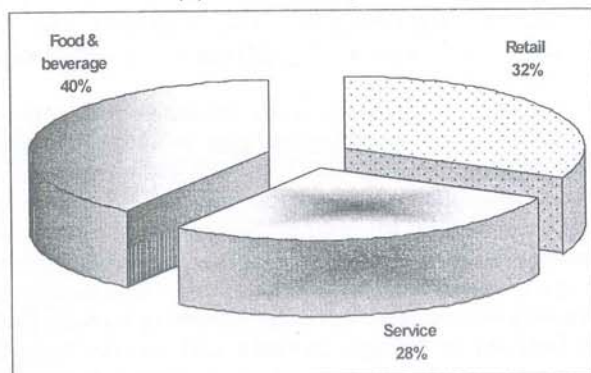
a. Food and beverage: This is one of the fields where the franchise develops at the fastest speed in Vietnam and other countries as well. Facts from international economic development show that other fields that experienced the same boom in franchise are auto services and retail stores. At present, franchises make their appearance in many other fields, such as hotel, real estate, jewelry, footwear, health care and education and they prove to be a successful way of doing business. However, the food supply is still the field where the franchise business gains the fastest development.

Statistical data from Japan – the world's third biggest market for franchise contracts with 1,100 systems of franchise that generate some US\$150 billion a year with a growth rate of 7% - show that the food supply accounts for 40% of the systems and 23% of stores where franchise exists.

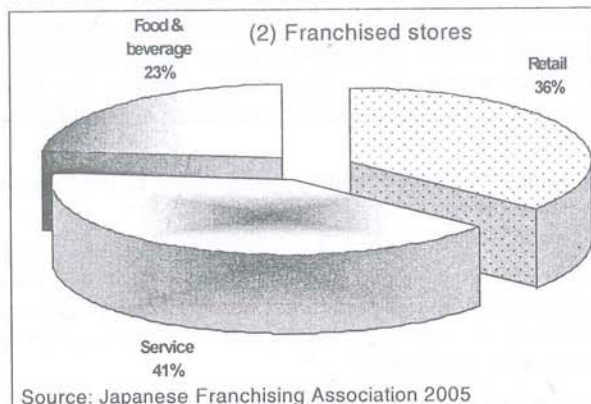
In Singapore in 2004, there were 380 franchised systems and 5,277 franchised stores and it is most common in the food and beverage business.

Figure 1: Franchise in Japanese food supply

(1) Franchised systems



(2) Franchised stores

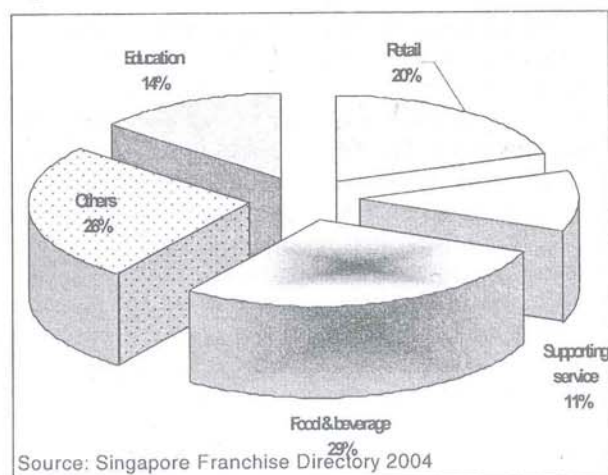


Source: Japanese Franchising Association 2005

In Vietnam, although there is no numerical data about franchise system in the food supply business, my survey shows that the best part of franchised systems in HCMC are in this field because it has many factors suitable to the franchise operation:

- Food supply store doesn't require as big investment as in hotels, real estates or supermarkets, which encourage owners to act as franchisees.

Figure 2: Franchised systems in Singapore



Source: Singapore Franchise Directory 2004

- Food is among basic needs of consumers, therefore the franchise in this field is the most common in all countries. This factor allows the existence of many food stores in the same districts, or even on the same streets, and one franchisor can cooperate with many franchisees.

- When the living standard is improved, the public usually wants better and more convenient food with the result that such brand names as McDonald's, Jollibee, KFC, and Lotteria expand and develop worldwide.

- Food reflects cultural features of individual province, region or country, therefore the food supply business not only meets a market demand but also helps disseminate local ways of eating and cooking and special dishes. This factor helps it get more opportunities to develop than other businesses do.

- Formula or recipe used by food franchisors are transferred more easily than ones in other fields.

b. Vietnamese franchised brand names: Among food and beverage franchisors are Trung Nguyên, Phở 24 and Kinh Đô. Trung Nguyên is the pioneer in franchising, and as a pioneer, it has met with many difficulties, especially in controlling uniformity of franchised cafés. It was followed by Kinh Đô Bakery chain store that was started in 2006 and is not much successful in its effort to open 100 stores by 2008. Phở 24 is the most successful and professional franchising system in Vietnam. It does business not only in Vietnam but also in many foreign countries.

c. Foreign franchised brand names in Vietnam: At present, the Yum! Group from the U.S. has franchised two of its famous brand names to local partners: KFC and Pizza Hut. Yum! Group has sold a master franchise to KFC Vietnam – a joint venture between Vietnamese and Singaporean partners – within a period of 25 years and another master franchise for Pizza Hut to the Pizza Hut Vietnam comprising IFB Holdings and Jardine Restaurant Group.

Besides these two brand names, the Jollibee from the Philippines opened six chain stores up to May 2005. The Australian Gloria Jean's Coffee has also entered the Vietnamese market by cooperating with Phong Cách Sống Việt Ltd and has opened two stores in Vietnam. It's necessary to mention the chain stores in many provinces supported by the Lotteria from South Korea. But this company hasn't franchised its brand names although its franchising plan has been worked out.

Ten years after the franchise business was introduced to Vietnam, it has made good progress in recent years, especially in the past three ones. Quantity and quality of franchising system are improved



continuously. Many "made in Vietnam" goods have established their footholds in foreign markets and many global brand names have entered Vietnam. Sales of franchised goods and services have increased remarkably in comparison with 1999-2000 and many new jobs have been created. Authorities have started paying attention to this business. Although this attention is not as suitable as expected, it also reflects the effort to encourage successful models introduced by all classes and sectors. This also means that the franchise is an inevitable part of the economic growth.

However, there are many problems with this business because it is still new to both authorities and business circles in Vietnam. The franchising business in the food and beverage field in HCMC has developed in an almost unruly manner and lacked professional features. Local companies usually fail to pay full attention to the building of brand names and an effective business model, protect and franchise them. Besides Phở 24, the only business proves to be professional in this activity, most local companies know almost nothing about this model, including ones in HCMC where exist many active companies that are eager to absorb new things and deal with business risks. Some companies have started their franchising plans but failed to maintain the uniformity of goods and services with the result that their networks get out of control and beyond repair. In addition, there is no cooperation between franchisors and banks in securing necessary capital for the franchising business. Regulations on the franchising business overlap with ones on laws of intellectual property, technology transfer and

commercial activities. Many companies still worry about protection for brand names as assets and settlement of disputes by law. This imperfect legal infrastructure causes a lot of difficulties and obstacles to the franchising business.

In reality, Vietnam lacks famous brand names suitable to the franchise business because the building of brand names didn't receive proper attention from managers. Moreover, they have no plan to take measures to protect their brand names in preparation for franchising. This is one shortcoming that prevents the development of this business. To secure their shares in the domestic market, find a foothold in foreign markets and survive foreign competition, local companies should review their plans to build brand names and trade marks as important assets. In HCMC, some companies have succeeded in building their brand names but they didn't feel confident enough to think of franchising them.

2. Measures to encourage franchise of local food and beverage

With its potentials, local companies can develop well the franchising business. Application of this activity to the food and beverage supplying business will help it to develop faster and contribute more to the economic growth.

Companies in this industry have many opportunities to succeed by building effective business models. To achieve this aim, companies should make the best use of their potentials and take advantages of various factors. Analyses of local franchisors and franchisees shows that they suffer numerous shortcomings: from building and protecting their brand names, ensuring uniformity of their goods and services, to developing new products and human resource. In my opinion, an effective business models for them should be based on the four following factors:

- Brand name: This is the most important factor in the franchise business because it is the most valuable asset one company can offer to sell besides its goods and know-how. The brand name helps the company win respect from not only customers but also potential franchisees. Before the company can franchise its goods or services, the company should carry out marketing campaigns to build brand names for its goods and services.

- Uniformity and consistency of the system: Building a system with uniformity and consistency is an important factor to the franchising plan. The uniformity not only creates the consistency for the business and the brand name but also helps the company franchise its goods and control its business easily.

- Goods and services: The company should not only produce goods that meet the market demand but also create some uniqueness for their goods before thinking of franchising them. The uniqueness doesn't mean that the product is totally new to the market, but it must have its own features. Phở 24 is a good example. Phở (Vietnamese noodle soup) is not a new product but the idea of having a bowl of phở in a noble and clean shop with excellent service and wireless connectivity is new and attractive to many customers. Coffee is not new but Passio (take-away coffee) offers ready-made and delicious cups of coffee totally different from instant coffee. If a company wants to franchise its goods or services it should carry out studies in order to make products that satisfy the market demand in a unique manner.

The food production is very sensitive business because products must not only satisfy tastes of consumers but also ensure hygienic standards, convenience and other requirements. Customers will vote by their feet if the products fail to meet these requirements.

The food company should invest in R&D activity in order to develop new products, differentiate them, and improve the product quality, thereby satisfy customers' need better and better.

- Know-how: Know-how is a secret knowledge of making a product in a way that others can't imitate. The know-how may lie in managerial skills. In the food industry, the know-how usually lie in ways of creating smell and taste. Some traditional spices give characteristics to KFC products. Phở 24 has its

own way of preparing the soup that satisfies the tastes of people from all provinces and regions. The Subway Fast Food Company knows how to make fast and fresh food.

At macroeconomic level, a cooperation between commercial banks and franchisors, and between authorities and franchisees, is much needed. The role of banks is to supply necessary capital to both franchisors and franchisees in expanding their businesses. They also connect owners of brand names with potential franchisees, and offer advice on legal issues and terms of franchise. Authorities can help with cooperation by creating legal infrastructure needed for these operations of banks. In such a connection, franchisees and franchisors may cooperate successfully through banks and authorities.

In addition, authorities and companies should deal with the following problems:

- Establishing an association of franchising companies in order to prepare conditions for new developments of the business.

- The Government should perfect regulations on the franchising business because many disputes may take place in relation between franchisors and franchisees.

- Authorities may give various incentives to this business by offering loans, advice and information, etc.

- Knowledge of franchising business can be included in teaching programs in universities and vocational schools in order to prepare a new wave of human resource for the business. ■

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