

Buying a McDonald's franchise

In this two-part series, **Paul Hoang** speaks to **Tonina Hoang** about buying, setting up and running a McDonald's franchise in the UK

Tonina and Keith Hoang are successful entrepreneurs who owned the rights to three franchised Chinese takeaway restaurants in London and Essex. So what made this husband and wife team want to give up their businesses and risk buying a McDonald's franchise?

What is franchising?

McDonald's, the world's largest fast food restaurant chain, has more than 12,000 outlets, with around 65% of them being franchised. A franchise is a form of business ownership whereby a person or business buys a licence to trade using another firm's name, including use of its logos, brands and trademarks. In return for this benefit, the purchaser of a franchise (called the franchisee) pays a licence fee to the parent company of the business (known as the franchisor). The franchisee is also required to pay a royalty payment (a percentage paid according to the value of sales made by the franchisee).

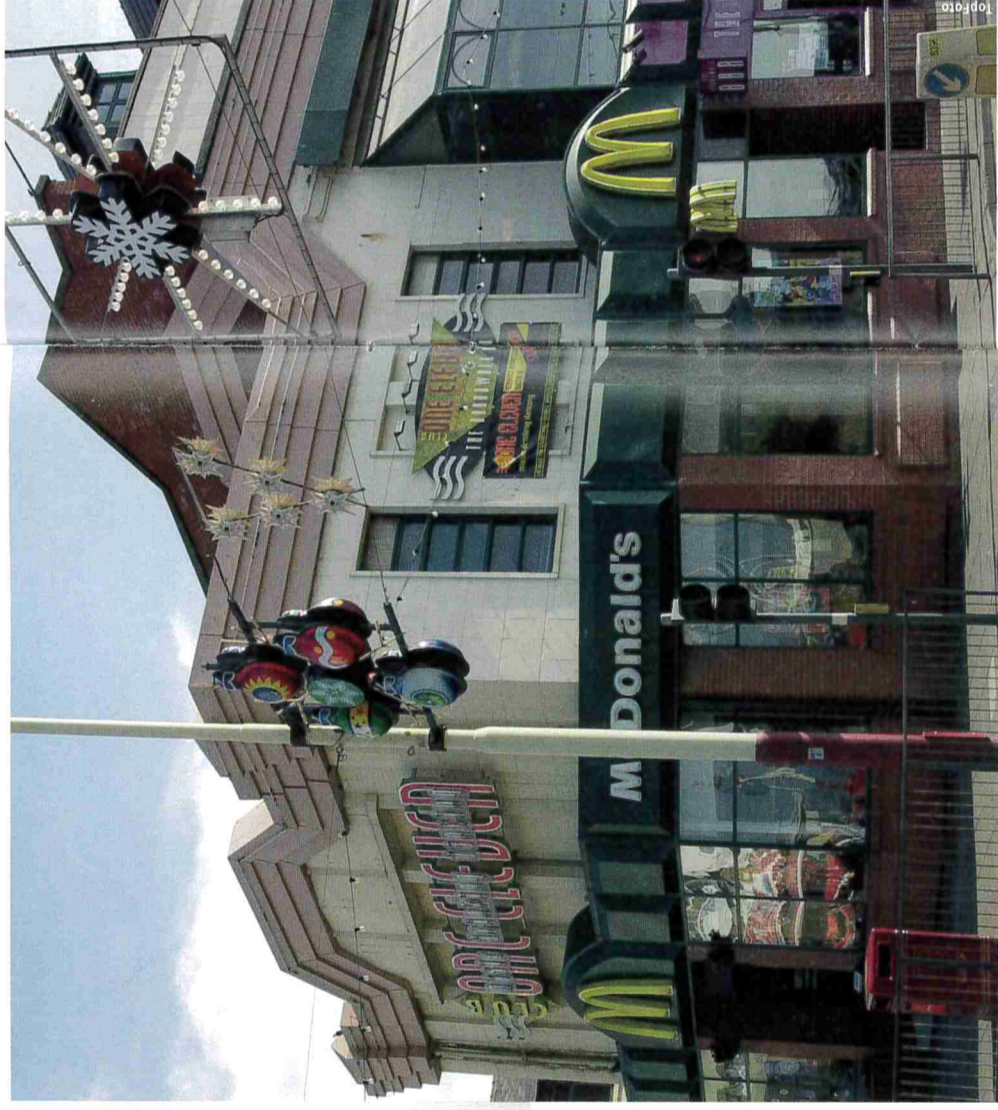
Franchising is a popular growth strategy for businesses both nationally and internationally. Its high success rate relies on the know-how, brand recognition and trust of a parent organisation coupled with the incentives and enthusiasm of the franchisee to make it a success. McDonald's uses franchising as a hybrid method of internal and external growth

The application process

Before McDonald's allows a franchisee to buy one of its restaurants, applicants have to go through an extensive and rigorous application process. For Tonina, this experience included:

- Tonina and Keith doing their own research and attending a franchisors' convention in Birmingham
- a formal application to McDonald's, which receives around 150 applications per month
- surviving a gruelling 3-hour interview

This was an unusual situation for Tonina, as she had been running her own business successfully for many years. She admits:



The interview was so extensive, I found myself asking for a comfort break — something I've never done before!

Those deemed suitable after the initial interview are offered a 5-day on-the-job experience (OJE) in a McDonald's restaurant, led by the restaurant's business manager. Tonina's OJE culminated in an evaluation from an 'operations consultant' (McDonald's supervisor) and the experience also provided opportunities for Tonina to talk to the management team to gather their perspectives, including succession planning, examining their ICT tools and reporting systems, and getting to grips with 'burgeromics' terminology.

Afterwards, potential franchisees are required to submit a detailed report on how the restaurant could increase its profitability, market share and customer satisfaction.

Not quite there yet

Successful candidates are invited for a second interview with the vice president of franchising for the region. Those deemed suitable after the second interview embark on a demanding 9-month training programme based in a McDonald's restaurant (for Tonina, this was at the Wandsworth Bridge store in London). A key purpose of this is to train the 'owner-operator' (franchisee) to business manager level.

During this process Tonina had to produce a detailed financial plan proving she had the necessary support structures in place

to sustain her family's expenses during the training programme. One reason for this is to allow potential franchisees to 'prototype' their new lifestyle.

Many people do not realise that potential franchisees have to pay for their own expenses during the application and training process. Tonina worked 12–14 hours a day, 6 days a week, being fully involved in the restaurant at Wandsworth Bridge, totally unpaid. In addition, potential franchisees are required to divest all other commercial interests to allow them to give their full attention and best efforts to the new business venture. In the interim, Keith continued managing the Chinese takeaways to support the family.

The outcome

In the year that Tonina applied for a McDonald's franchise, only three applicants were accepted onto the programme (the other two were based in Manchester and Scotland). Tonina graduated from the training as part of the (rather small) class of 2010.

At the time of writing, around 75% of 1,200 McDonald's restaurants in the UK are franchised. On average, each McDonald's franchisee owns four restaurants. Tonina agreed to the terms and conditions of her first McDonald's franchise, located in Bromley High Street, in October 2011.

Benefits of franchising

The benefits for McDonald's, the franchisor, include:

- The parent company can experience rapid growth without having to risk huge amounts of money, as the franchisee pays for the outlet itself and all personal expenses during the application and training process. The potential franchisee pays a £5,000 deposit to take part in the programme, deductible from the restaurant purchase price if the applicant is successful. The purchase price of a McDonald's franchise restaurant depends on two closely related variables: the annual sales revenue of the restaurant and its location.

- Franchising allows McDonald's to have an international presence without the costs of organic growth or takeovers, as the franchisees help to finance the expansion. Hence, franchising is less risky for McDonald's than internal growth.

- McDonald's can benefit from growth without having to worry about running costs such as staff wages, purchase of stock and recruitment. These are paid for by the franchisee.

- McDonald's gains from economies of scale, as franchising is a relatively fast method of business growth. The business also gains from the entrepreneurial ideas of franchisees.

- McDonald's receives royalty payments from the franchisee, usually set as a percentage of the sales revenues. It may also charge a 'membership' (administrative or joining) fee to its franchisees.
- Franchisees have more incentives to perform than salaried McDonald's store managers (employees), thereby increasing the chances of success for the organisation.

- Local franchisees will have a greater awareness of local market conditions and possible cultural differences. In the second part of this series I will look at Tonina's involvement with the local community, including her town team bid for £10,000 from the Portas Pilot for Bromley, part of a government initiative to revive ailing high streets through localism.

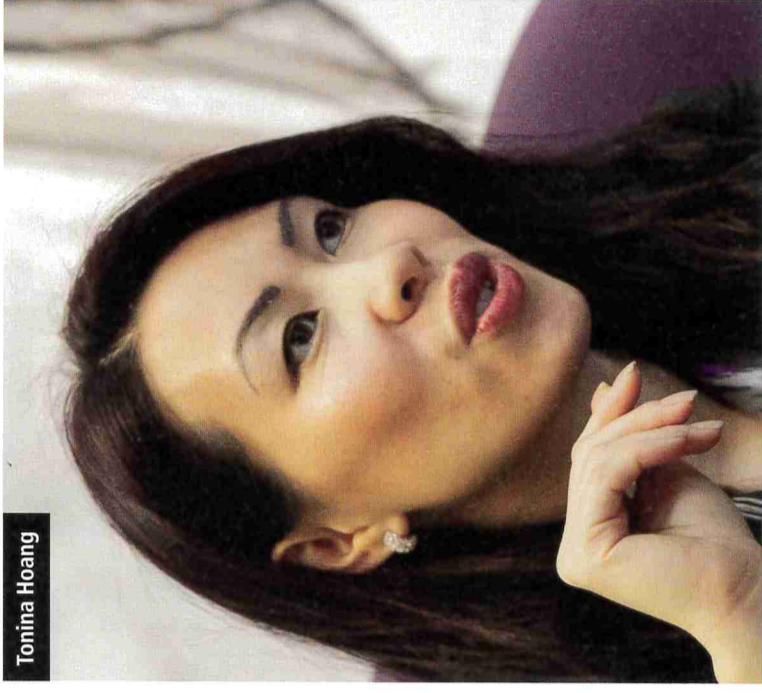
Franchising also has advantages for the franchisee. Tonina was driven by the opportunity to work with a global brand and expand during the credit crunch. She also wanted a new challenge, having worked in the Chinese takeaway industry for 10 years. Other benefits of operating as a McDonald's franchisee include:

- The McDonald's business model is tried and tested, so presents a relatively low-risk investment for the franchisee. The chances of success are much higher than setting up a restaurant from scratch.
- The start-up costs are relatively low because the business idea has already been developed by the franchisor.

- It is in the franchisor's best interests to ensure that the franchisee succeeds. This means that the franchisor will provide extra services to the franchisee, such as training and advice on financial management. Each McDonald's franchisee is assigned a field services consultant who provides ongoing support services and helps to ensure McDonald's fulfils its side of the franchise agreement.

- The franchisee is likely to benefit from large-scale marketing used by the well-known parent company. In the case of McDonald's, franchisees pay a contribution towards national

Tonina Hoang



- Franchisees have to pay a significant percentage of their revenues to the franchisor. The amount depends on numerous factors based on affordability, i.e. what McDonald's thinks the franchisee can afford to pay based on projected sales figures.
- Franchisees cannot use their own initiative to try out new ideas. For example, a franchisee would not be permitted to launch a new product without going through McDonald's' extensive product development processes.

Conclusion

Buying and setting up a McDonald's franchise is certainly no easy task. Despite the pitfalls, Tonina and Keith have recently secured their second franchised McDonald's restaurant, at the Glades Shopping Centre in Bromley. When asked whether she ever had second thoughts about the franchise, Tonina's response was:

For sure! There have been some challenging times during the 9 months training as well as during the first year of owning the restaurant where I had very seriously considered a life outside McDonald's. Four years on and I'm really 'lovin' it' and there's nothing else I'd rather be doing.

She just couldn't resist the tagline, could she?

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advertising. The national marketing fees are paid to a separate marketing agency (McMarCo), which is chaired by a franchisee. This committee consists of around five franchisees and two McDonald's executives. Franchisees receive national exposure from McDonald's marketing, thereby helping to reduce the overall costs of advertising and promotion.

- Working regular hours — instead of the 'graveyard shifts' of the Chinese takeaway industry — was a key reason for Tonina, as she has three young daughters.

Franchising pitfalls

There are several potential disadvantages for McDonald's as a franchisor:

- It may prove difficult to control the activities of all franchisees and get them to meet the quality standards required.
- McDonald's takes a huge risk in allowing others to use its brand name. Franchisees who do not follow the established systems or do not meet expectations may end up harming the reputation of the whole organisation.
- Although franchising is faster than organic growth, the process is still not as quick as mergers or takeovers. In Tonina's case, the application process, training and transfer of ownership of a McDonald's restaurant took around 20 months.

The disadvantages for franchisees like Tonina include:

- Buying a franchise can be relatively expensive, as the franchisee is paying for 'goodwill' from McDonald's. There is no guarantee that this money will ever be recouped.

