

# THE VALUE OF FRANCHISING

Franchises represent an alternative to traditional forms of business operations. Through a legal agreement, the franchisee sells a product or service using the brand name or operating system (or both) of the franchisor, typically in return for a lump sum payment and annual royalty fee. Most people immediately associate franchising with fast food restaurants. Interestingly, however, quick service restaurants are just a fraction of the entire sector, making up only a fourth of all franchised establishments, less than half of the workers, and just over a third of the economic output.

In commissioning this study, the International Franchise Association asked Oxford Economics to examine the value of the franchising model along a range of dimensions. We had three goals for this research:

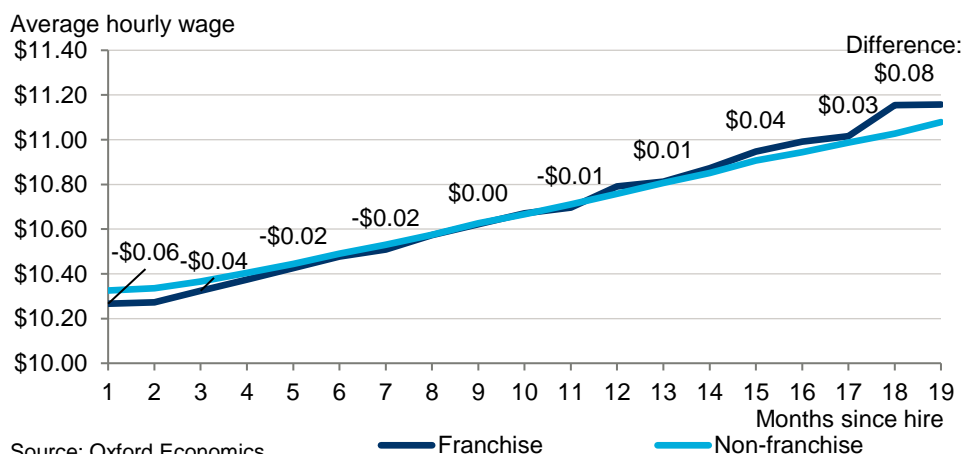
- 1 Analyze pay, benefits, and training** at franchised firms and compare these attributes with similar non-franchise employers where possible
- 2 Assess franchising as a path to entrepreneurship** and uncover areas where the business model provides vital support to prospective business owners
- 3 Understand how franchisees are embedded in their local communities** by examining their supply chains and charitable giving

## FRANCHISES OFFER PAY, BENEFITS, AND TRAINING ON PAR WITH COMPARABLE NON-FRANCHISE SMALL BUSINESSES

To see how wages at franchise firms stack up, we explore wage data from a sample of 3,700 franchise and 137,000 non-franchise small businesses, drawn from a payroll database. An econometric analysis of workers' wages controlling for a variety of factors finds that workers at franchise firms earn slightly more than workers at non-franchise firms, although the difference is statistically insignificant. This is consistent with existing academic research, including Cappelli and Hamori (2008) and Kruger (1991). Franchise firms in our dataset are somewhat larger on average (13.6 versus 9.6 distinct workers per month), in line with results from the 2016 Annual Survey of Entrepreneurs.

An analysis of newly hired workers also finds that starting wages, wage growth, and worker turnover are extremely close between franchises and non-franchises (Fig. 1), while franchise workers were somewhat more likely to be promoted to manager (14% of remaining workers after 19 months vs. 11% at non-franchises).

**Fig. 1. Average hourly wage progression since hiring date, franchise vs. non-franchise**



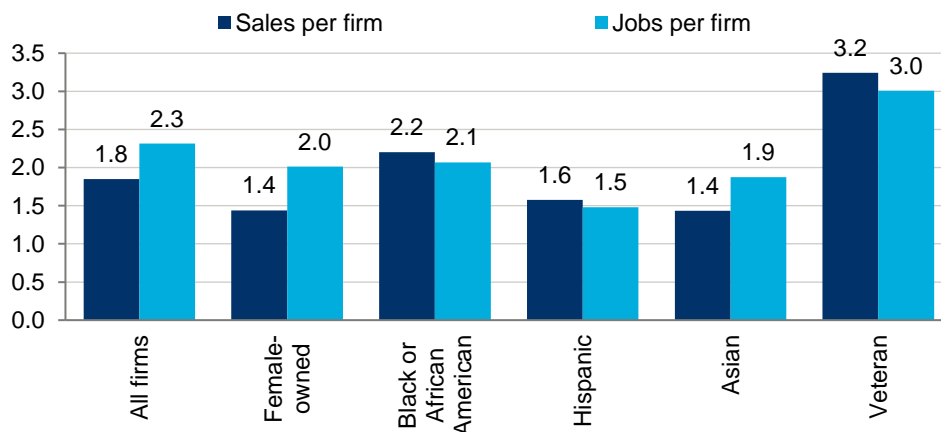
In addition to the payroll database, we look at the non-wage component of employee compensation using a survey of franchisees completed by over 4,000 respondents (hereafter referred to as the Franchise census). We find that the share of workers that is offered various types of benefits at small franchised firms is roughly on a par with the share of employees with access to those benefits at small US establishments.

Franchises also appear to offer training to a very similar extent to the average US business. According to the Association for Talent Development, in 2019 each US employee used 34.7 hours of formal learning on average. The Franchise census suggests franchisees offer an average of 33.4 hours of formal training per employee, with 11% of respondents offering 50 hours or more per worker.

### FRANCHISING OFFERS A PATH TO ENTREPRENEURSHIP TO ALL AMERICANS, BUT ESPECIALLY TO NEW ENTREPRENEURS AND WOMEN

The 2016 Annual Survey of Entrepreneurs (ASE) suggests that franchise businesses tend to be larger than non-franchise businesses. We find that, on average, franchises report sales 1.8 times as large as non-franchise businesses and provide 2.3 times as many jobs as non-franchise businesses. Sales and jobs in franchised businesses exceed non-franchised businesses across all demographic cuts, including gender and race. For example, Black-owned franchise firms earn 2.2 times as much in sales compared to Black-owned non-franchise businesses, on average (Fig. 2).

**Fig. 2. Ratio of average sales per firm and jobs per firm, franchise vs. non franchise business**



Source: ASE (2016)

What factors enable franchised businesses to reach a larger scale? The Franchise census asks franchisees to describe the areas where franchisor support was received and proved most useful. Results suggest the most important areas are franchisee training, meetings and events, and technology platforms. Even in areas where franchisor support is less widespread, such as access to capital support (received by 42% of respondents), the positive effects of the business model are striking. Some 21% of respondents report being capital constrained when starting their first franchise business and that being a franchisee provided them with access to capital.

In addition, 32% of all respondents report they would not own a business if they were not franchisees. This proportion is even greater among both female owners and owners for whom a franchise was their first business (39%). When applied to the total number of franchise firms from the 2016 ASE, this would be equivalent to a loss of 60,000 businesses (or nearly 223,000 establishments, employing some 1.8 million workers) if franchising was not an option.

## **FRANCHISES ARE LOCALLY OWNED AND THIS KEEPS RESOURCES IN THE LOCAL COMMUNITY**

Unlike the multi-unit company-owned business model, franchises allow franchisees to buy and own the units they operate. By doing so, franchisees essentially become small business owners, who live and work in their communities. The brands they represent do not ship workers in from other parts of the country, but rather franchisees recruit and train local residents. The franchise model therefore encourages local employment and wealth-sharing with local communities.

The Franchise census suggests franchisees purchase 21% of their inputs from local suppliers, indirectly contributing to their local economies through their supply chains. Over a third of respondents (36%) purchase at least 25% of their intermediate goods locally.

In addition, some 65% of franchisees give to local charities according to the Franchise census. This is in line with findings that suggest 66% of small businesses do so. Among donors, franchisees donate an average of 6% of their profits (also in line with small businesses' data). We estimate that US-based companies operating as franchises jointly donated a total of \$1.5 billion to charity in the year before the pandemic and raised over \$900 million over the same period. Some 18 million hours of volunteering were sponsored by franchised businesses in 2019, which are worth hundreds of thousands of dollars to society more broadly.

In conclusion, this study finds that franchises offer wages, benefits, and training on par with similar non-franchise small companies. We also show that franchising offers a path to entrepreneurship to all Americans, but particularly to first-time owners and women. Lastly, we highlight how franchisees are embedded in their local communities through their local supply chains and charitable giving.

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