

**STRATEGY OF FRANCHISE SUBCONTRACTING AND  
SUSTAINABILITY OF SMALL AND MEDIUM ENTERPRISES IN  
SELECTED COUNTIES IN KENYA**

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## DECLARATION

This research is my original work and has not been presented for award of any degree in any University.

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## **DEDICATION**

I dedicate this project to my dear wife Eunice and Children Victor and Joy.

## **ACKNOWLEDGMENTS**

I take this opportunity to give thanks to the Almighty God who enabled me through this project. Special thanks to my Supervisor Mr. Eliud Mududa for the guidance, encouragement, patience and understanding while working on my project. I also appreciate in a special way the moral support from my family. Thanks to my friends Mercy, Cyrus, Mawazo and others who played very important support in making this project a great success

# TABLE OF CONTENTS

<b>DECLARATION</b> .....	<b>ii</b>
<b>DEDICATION</b> .....	<b>iii</b>
<b>ACKNOWLEDGMENTS</b> .....	<b>iv</b>
<b>TABLE OF CONTENTS</b> .....	<b>v</b>
<b>LIST OF TABLES</b> .....	<b>viii</b>
<b>LIST OF FIGURES</b> .....	<b>ix</b>
<b>ABBREVIATIONS AND ACRONYMS</b> .....	<b>x</b>
<b>ABSTRACT</b> .....	<b>xi</b>
<b>CHAPTER ONE: INTRODUCTION</b> .....	<b>1</b>
1.1 Background .....	1
1.1.1 Concept of Strategy .....	2
1.1.2 Franchise Subcontracting strategy .....	3
1.1.3 Strategy and Sustainability of Organizations.....	4
1.1.4 Structure of County governments in Kenya .....	5
1.1.5 SMEs in the selected Counties in Kenya .....	5
1.2 Research Problem.....	6
1.3 Research Objectives .....	8
1.4 Value of the study .....	9
<b>CHAPTER TWO: LITERATURE REVIEW</b> .....	<b>10</b>
2.1 Introduction .....	10
2.2 Theoretical Foundation .....	10
2.2.1 Resource Scarcity theory .....	10
2.2.2 Agency Theory .....	11
2.3 Franchise subcontracting concept .....	12
2.4 Sustainability of SMEs.....	15

<b>CHAPTER THREE: RESEARCH METHODOLOGY .....</b>	<b>17</b>
3.1 Introduction .....	17
3.2 Research Design.....	17
3.3 Target Population of the study .....	17
3.4 Sampling .....	18
3.5 Data Collection.....	18
3.6 Data Analysis .....	19
<b>CHAPTER FOUR: DATA ANALYSIS RESULTS AND DISCUSSION .....</b>	<b>20</b>
4.1 Introduction .....	20
4.2 Response rate .....	20
4.3 Background information .....	20
4.3.1 Type of business .....	20
4.3.2 Business ownership.....	21
4.3.3 Respondent’s position in the business .....	21
4.3.4 Startup capital .....	22
4.4 Adoption of franchising subcontracting.....	22
4.4.1 Business inception .....	22
4.4.2 Awareness of franchise subcontracting .....	23
4.4.2 Target of franchise subcontracting .....	24
4.4.3 Likelihood of more businesses operating under franchise subcontracting .....	24
4.4.4 Likelihood of new businesses operating under franchise subcontracting.....	25
4.4.5 Number of new businesses operating franchise arrangement.....	25
4.4.6 Market penetration of businesses under franchise subcontract .....	26
4.5 Sustainability of franchise subcontracting as a strategy .....	26
4.5.1 Competitive advantage of businesses operating on franchise subcontracting.....	26
4.5.2 Survival of businesses operating franchise subcontracting .....	27

4.5.3 Marketing support and supervision .....	28
4.5.4 Profitability of small and medium businesses .....	28
4.5.5 Profitability of franchise businesses .....	29
4.5.6 Contribution of franchising to business success .....	30
4.5.7 Likelihood of converting to freelance model.....	30
4.5.8 Likelihood of business surviving its 20th anniversary .....	31
4.5.9 Effect of franchising on sustainability .....	31
<b>CHAPTER FIVE:SUMMARY, CONCLUSION AND RECOMMENDATIONS .....</b>	<b>34</b>
5.1 Introduction .....	34
5.2 Summary .....	34
5.2.1 Adoption of franchising subcontracting .....	34
5.2.2 Sustainability of franchise subcontracting as a strategy .....	34
5.3 Conclusion .....	35
5.4 Recommendations and implications on policy, practice and theory .....	<b>36</b>
5.5 Limitations of the study.....	<b>36</b>
<b>REFERENCES.....</b>	<b>38</b>
<b>APPENDICES .....</b>	<b>42</b>
APPENDIX I : LETTER OF INTRODUCTION .....	42
APPENDIX II: RESEARCH QUESTIONNAIRE .....	43

## LIST OF TABLES

<b>Table 4.1</b> Business ownership .....	21
<b>Table 4.2</b> Respondent's position in the business .....	21
<b>Table 4.3</b> Business inception .....	23
<b>Table 4.4</b> Target of franchise subcontracting .....	24
<b>Table 4.5</b> Number of new businesses operating franchise arrangement .....	25
<b>Table 4.6</b> Competitive advantage of businesses operating franchise subcontracting .....	27
<b>Table 4.7</b> Survival of businesses operating franchise subcontracting .....	27
<b>Table 4.8</b> Profitability of small and medium businesses .....	29
<b>Table 4.9</b> Contribution of franchising to business success .....	30
<b>Table 4.10</b> Likelihood of converting to freelance model .....	30
<b>Table 4.11</b> Likelihood of business surviving its 20th anniversary .....	31
<b>Table 4.12</b> Effect of franchising on sustainability .....	33



## LIST OF FIGURES

<b>Figure 4.1</b> Type of business .....	20
<b>Figure 4.2</b> Startup capital .....	22
<b>Figure 4.3</b> Awareness of franchise subcontracting .....	23
<b>Figure 4.4</b> Likelihood of more businesses operating under franchise subcontracting .....	24
<b>Figure 4.5</b> Likelihood of new businesses operating under franchise subcontracting.....	25
<b>Figure 4.6</b> Market penetration of businesses under franchise subcontract .....	26
<b>Figure 4.7</b> Marketing support and supervision .....	28
<b>Figure 4.8</b> Profitability of franchise businesses .....	29

## **ABBREVIATIONS AND ACRONYMNS**

<b>EDS</b>	Every Dealer Survey
<b>EU</b>	European Union
<b>DOS</b>	Distributor Operating Standards
<b>SME</b>	Small and Medium Enterprises.

## ABSTRACT

Whereas the strategy of franchising is hundreds of years old in the global market, until recently, the franchise business model has been slow to take hold in Kenya because local investors know little or nothing about its potential rewards. It is therefore on this basis that this study sought to address the question; “Can Strategy of franchise subcontracting mitigate or eliminate the sustainability challenges faced by SMEs in the selected Counties in Kenya?”. Specifically, the study sought to determine the extent of adoption of franchise subcontracting as a strategy by SMEs and to determine the viability of such a strategy in the sustainability of small and medium enterprises. This study was descriptive in nature and a survey design was applied. In this study the target population was about 300 SMEs operating within the franchise subcontracting strategy in the major urban centers in Laikipia, Embu and Meru counties. This study used the stratified random sampling technique to draw a sample of 100 SMEs. The target respondents was the business owners of the sampled enterprises or the top manager in the enterprise where the owner of the business may not be available to respond. Data was collected through structured questionnaires. The qualitative data was analyzed manually by first summarizing the information gathered followed by categorization and coding into emerging themes. The study found that the number of new small and medium businesses operating under a franchise subcontract arrangement was increasing in the previous two years prior to the study and there was a high likelihood that more small and medium business men will start new businesses within a franchise subcontracting agreement in the following two years. It was also found that apart from gaining competitive advantage and increasing profitability, most small and medium businesses operating under franchise subcontracting agreements were known to have survived the lifetime of their owners. In addition there was a very high likelihood that the business they were operating then would survive its 20th anniversary. It was therefore concluded that adoption of franchising subcontracting strategy is gaining high adoption among small and medium enterprises in the market. In addition, the study concluded that sustainability of SMEs operating under franchise subcontracting strategy is high. The study recommended that more companies should adopt the franchise strategy to increase their profitability. This is because the number companies currently operating franchises in Nyeri, Laikipia, Embu and Meru Counties is low compared to the total number of companies in the country.

# CHAPTER ONE

## INTRODUCTION

### 1.1 Background

Establishment of sustainable Small and medium business enterprises is perhaps the solution to the mind boggling economic recovery agenda world over. Whereas studies and solution searching to the sustainability issue has in the recent past reached desirable levels, emphasis has been laid on the challenges and factors affecting sustainability of such enterprises. Little has been done in evaluating the effectiveness of the recommendations as implemented in various economies. Besides, there is also very little literature to show how strategy has been applied to the sustainability problem for SMEs in many economies. Franchising strategy is one of those strategies which have been established overtime and has been used by multinationals to venture into new markets. There is now a trend in the market for franchised businesses extending their franchise agreements to other agencies notably Small and Medium enterprises for collaboration for value. This study will seek to find out whether the collaborative value on the side of the SMEs confers sustainability to their businesses.

Strategies in business are by and large supported by theoretical propositions. Such theories show how the birth of a given strategy connects to the root economic challenge or problem existing at the time. A number of theories have been suggested as backing the strategy of franchising. In this study, two key theories will be discussed:- the resource scarcity theory(Oxenfeldt and Kelly, 1996 ) and the agency theory (Jensen & Meckling, 1976 ). In a nutshell the resource scarcity theory implies that the strategy of franchising emanates from the franchisor's financial problem hence the franchisor extends his business rights to other entrepreneurs who have the money to further the franchisors business at a cheaper cost. The agency theory on the other hand presents a common argument in modern business that the principal (Franchisor), in view of the need to concentrate on his core business lets out part of his business rights to agents (Franchisees) who complete the franchisors business at a lower level of the business supply chain. The theory further brings out two major agency problems that entangle the strategy of franchising.

Whereas the strategy of franchising is hundreds of years old in the global market, until recently, the franchise business model has been slow to take hold in Kenya because local investors know little or nothing about its potential rewards, industry insiders say. However, American franchises such as KFC and Naked Pizza have begun to pop up in Nairobi. Given the establishment of the counties, investment prospects outside of Nairobi are likely to emerge in the coming years. While a number of studies have been conducted about franchising in Kenya, more focus has been given to the major cities and more specifically in Nairobi.(Mboloi,2007; Okatch et.al 2011). This study will focus on four selected counties:- Nyeri, Laikipia, Embu and Meru Counties. The selected counties form a key economic hub in Kenya in that besides the large number of populations that each of them supports, these counties are located on one of the country's major agricultural zones. Without undue emphasis, the new constitutional dispensation spells a new economic outlook. As more resources get devolved to the counties, there is need to establish critical economic truths and prepare the entrepreneurs for the eminent gainful future and economic growth. It is on this basis that a few potential counties were selected for this study.

### **1.1.1 Concept of Strategy**

The debate about what strategy is and what it is not is never ending. In his early writings on business strategy, Michael Porter builds around such terms as unique positioning of a business to gain competitive advantage against competition. Porter (1996), explains strategy as on the one hand, choice (i.e., having a bundle of options of how to lead a company into the future) and, on the other hand, uniqueness (i.e., deliberately choosing a different set of activities to deliver a unique mix of value). The fact that a turbulent business environment often causes paradigm shifts in the business landscape may require constant change in the way firms position themselves hence the argument that many firms and Managers are unable to distinguish between operational effectiveness and strategy. Nevertheless, various studies have tended to qualify strategy on the basis of how long the plan of action is able to sustain competitive advantage. Thus, one could argue that operational effectiveness is short term while strategy is the unique actions that give a firm a long-term competitive advantage over other firms.

In his view, Chandler (1962) defined strategy as a representation of the determination of an organization's basic long term goals and objectives and the adoption of courses of action and the allocation of the resources necessary for achieving those goals. For this matter, strategy is a process of systematic plan of actions sticking out to the future. Similarly, Andrews (1971) simply presents strategy as a pattern of major objectives, purposes, or goals and essential policies and plans for achieving those goals, stated in such a way as to define what business the company is in or is to be in and the kind of company it is or is to be.

More recent research introduces a strategy's "fit" with the firm's internal resources and capabilities. The resource-based view of the firm posits that an organization's unique, valuable, and difficult to replicate resources and capabilities form the basis for sustainable competitive advantage (Amit & Schoemaker 1993; Dierickx & Cool 1989). A most recent article by the Harvard business magazine (2014) defined strategy as simply a method or plan chosen to bring about a desired future, such as achievement of a goal or solution to a problem. It is in light of this definition that this study will seek to identify the characteristics of franchise subcontracting and how such characteristics qualify to solve the sustainability problems of SMEs.

### **1.1.2 Franchise Subcontracting strategy**

There have been numerous debates on the issue of franchise definitions (Hoy and Stanworth, 2002) but a broad definition, framed to meet the points commonly raised in debates, has defined franchising as; a business form essentially consisting of an organization (the franchisor) with a market-tested business package centered on a product or service, entering into a contractual relationship with franchisees, typically self-financed and owner-managed small firms, operating under the franchisor's trade name to produce and/or market goods or services according to a format specified by the franchisor (Stanworth and Curran, 1999). Franchising as a business format presents almost perfect formal network as it makes it possible for a well formulated business idea to spread and benefit millions of entrepreneurs across diverse geographical regions.

Franchise subcontracting has been practiced over time. Moreover, this strategy is gaining popularity in developing economies within the wider franchising and outsourcing strategies. Big firms for their need to be more efficient contract-out part(s) of their supply chain in order to concentrate and focus key resources on their core business. Franchise subcontracting is therefore an extension of a business franchise rights to a different business entity to contact specified business in a manner regulated by the franchisor.

For example a manufacturing franchise, such as a soft- drink bottling plant, gives a business person the right to produce and distribute the manufacturer's products, using supplies purchased from the franchisor. The bottling plant can further subcontract the distribution of the franchisor's products to smaller business entrepreneurs who must operate within specified business standards. A product franchise gives an entrepreneur the right to sell trade-marked goods, which are purchased from the franchisor and resold. Car dealers and gasoline stations fall into this category. The strategy of franchise subcontracting is thus a collaborative strategy where the franchisor, the franchisee and other subcontracted agencies mutually benefit and protect the interests of each other. Arguably therefore, the strategy of franchise subcontracting formulates a strong chain of business ideas and format which give the participants sustainability capability.

### **1.1.3 Strategy and Sustainability of Organizations**

For business enterprises, sustainability is the ability of a company to develop and implement winning plans and actions that lead to long-term success. The reality check that business entrepreneurs get is that when it comes to achieving sustainability, there's no silver bullet or magic pill to suddenly make a company be able to manage sustainability, and therefore be more profitable and secure on a permanent basis. It takes real work, in terms of being open for necessary change, committing to a plan, and the ability for the business manager to be able to determine and apply appropriate long term action plans. Sustainable establishment and development for organizations therefore means adopting business strategies and activities that meet the needs of the enterprise and its stakeholders today. According to Delloitte (1992), the concept of sustainable business development though progressively receiving growing recognition is still is a new idea for many small and medium business executives. For most, the concept remains abstract and theoretical.

While business traditionally seeks precision and practicality as the basis for its planning efforts, sustainable development is a concept that is not amenable to simple and universal definition. As Froschheiser (2007) puts it, “It is fluid, and changes over time in response to increased information and society’s evolving priorities”. This argument fits well in building a serious case for strategy in the business sustainability agenda. Simply put, organizations can no longer survive sustainably within the traditional business practices in view of the characteristic environmental turbulence in today’s business environment. Suffice it to say therefore that strategy and sustainability of organizations are inseparable.

#### **1.1.4 Structure of County governments in Kenya**

The county is a newly formed political and economic jurisdiction in Kenya. There are 47 counties in Kenya out of which four (4) of them have been selected for this study namely Nyeri, Laikipia, Embu and Meru. Basically, the governance structure of the county is composed of two arms i.e the county assembly and the Executive. The county assembly is charged with the principal mandate of formulation of county laws and policy while the executives’ principal mandate is the implementation of county function policies.

Regulation of matters of trade and industry in the county falls within the executive and administered by a county executive member appointed by the Governor. Whereas implementation of the county functions as laid out in the Kenyan constitution is still ongoing, the administration of economic affairs is still wanting. Licensing of trade including for small and medium enterprises in the counties is by and large riding on the former municipal councils’ regulations of the Single business permit. No new policy framework has been put in place in the counties to address the SMEs challenges.

#### **1.1.5 SMEs in the selected Counties in Kenya**

There is no single criterion universally adopted in defining SMEs mainly because of the wide diversity of businesses and economic contexts. There exist a big number of category threshold definitions by different institutions and authorities. Nevertheless, almost all the criteria used by the different institutions and economies have something in common:- the parameters are based on the number of employees a firm establishes and the annual turnover. Perhaps the definition by the Bolton Committee in its 1971 report on Small firms can be seen as the best



definition so far used. According to the Bolton committee, an SME is an independent business managed by its owner or part owners and having a small market share. The Bolton definition has also been used by Recklies, (2001). The Bolton definition has been adopted for use in this paper.

In the counties selected for this study SMEs are both in the formal and informal sectors and spread through all industries. These enterprises provide one of the most prolific sources of employment creation, income generation and poverty reduction in the counties. According to Wikipedia (2014), there is a wide range of largely unsophisticated light industries, including motor vehicle repair garages, electronics repair shops, furniture workshops, tailoring shops, and bakeries in Nyeri County which are basically SMEs. A preliminary survey in Nyeri, Nanyuki, Embu and Meru towns indicated that the area has concentration of SMEs in hardware businesses for building materials, electronics, food stores, hotels, manufacturing businesses especially in milk and soft beverages. There is also a high concentration of fuel and gas stations, beer and soft drinks distribution businesses. A number of these businesses are run within franchise agreements between owners and established large franchises. The owners of these businesses in the region are spread within the full range of social classes and demographics.

## **1.2 Research Problem**

Sustainability of SMEs has been a topic of concern for some time. Various intervention measures have been suggested through studies to this effect (Parera et.al, 2013, Tinker 19997) Notwithstanding, SMEs continue to face sustainability challenges. Perhaps strategy is the solution to the sustainability challenges for small and medium enterprises. From the writings of Michael porter, strategy can be interpreted as the unique positioning of an organization's course of action to confer competitive advantage for her products against its competitors. Furthermore, strategy as opposed to operational effectiveness is concerned with those actions or business plans and approaches that span over the long-term translating to sustainable existence. Arguably therefore, there seems to be a direct link between sustainability (long term survival) of businesses and strategy.

In Kenya and more so in the counties selected for this study, small and medium entrepreneurs have continued to grapple with effects of unsustainable investments. According to the Kenya bureau of statistics (2007), 60% of small businesses established in Kenya fail within the first year of establishment. Such rate of business failure is alarming and therefore the need to further investigate the causes of failure and effects of different strategies applied remains fundamental. Notably, the strategy of franchise subcontracting is gaining popularity in the four counties. Preliminary survey has indicated that there is well over 400 small and medium enterprises established within a franchise subcontract. It is in this regard that such gain in popularity attracts the attention to explore the strategy adoption and its suitability in the sustainability of SMEs.

A common conclusion by several studies on SMEs in Kenya has created a strong impression that key to the issues that threaten the growth and sustainable development of SMEs is lack of financial credit facilities and poor or lack of favorable policy framework for SMEs ( Morara et al.2009). In response to such findings, the government of Kenya for instance has put notable intervention measures. Sessional paper No. 2 of 2005 clearly sets out clear SME financing strategies and policy guidelines which have largely changed the SMEs landscape especially in the area of financing and policy for protection of SMEs from unfair competition by large firms.

Recent studies have focused on strategy in search for the badly needed sustainability solution. A study by Nyang'ori (2013) supports another by Chuthamas (2011) in suggesting that SMEs should leverage the advantages of being small by deploying the relationship marketing strategy. By establishing long-term relationships with customers they are able to build customer loyalty and in turn reduce the cost of operation hence become sustainable. Nyang'ori further discusses the relationship strategy to include collaboration with local authorities for policy framework. In his study, Kagwathi et al. (2013) found out that risk mitigation strategies were key for the sustainability of SMEs. The study argues that most SMEs in Nairobi Kenya fail to survive as a result non- mitigated risks such as customer creditworthiness, burglary and theft among others. However, this study concentrates on continuity of business in the event of emergent calamities or misfortunes and does not clearly

discuss survival of businesses within normal course of operations. Another study by Njau (2010) reported that many SMEs owners run more than one business as a diversification strategy to manage risk but that the process could be improved if SMEs managers were skilled the choice of suitable business combinations in their portfolios.

Anantadjaya et al (2007) in evaluating the application of innovation strategies for SMEs established that in order to maintain existence in the marketplaces, entrepreneurs of SME may have to concentrate on engaging in the similar/complimentary products, investments, coming up with innovation, establishing ventures, and take benefits on the fluctuations on interest rates. Yet SMEs in their inherent smallness lack the muscles to take on any meaningful innovations against their large counterparts. Closely related studies have been undertaken by Mboloi (2007) on challenges faced by franchised Pharmaceuticals while Okatch et.al (2011) evaluated the how firm benefits influence franchise subcontracting in the Motor vehicle industry in Nairobi Kenya. In this study Okatch concludes that institutional and policy support was required to moderate the industry and give local assemblers some competitive edge over their multinational competition.

As can be seen, the above studies have not tackled the strategy of franchise subcontracting for the purpose of sustainability of SMEs especially in the selected counties and that intervention measures following such studies do not seem to have resolved SME sustainability issues. It is therefore on this basis that this study sought to address the question; “Can Strategy of franchise subcontracting mitigate or eliminate the sustainability challenges faced by SMEs in the selected Counties in Kenya?”

### **1.3 Research Objectives**

The objectives of this study were;

- i. To determine the extent of adoption of franchise subcontracting as a strategy by SMEs in the selected counties
- ii. To determine the viability of such a strategy in the sustainability of small and medium enterprises.

#### **1.4 Value of the study**

This study will seek to add value in three dimensions. First, the policy framework on SMEs and their sustainability is elaborate in Kenya.(Sessional paper No. 2, 2005). Besides, vision 2030 further articulates the direction in the course of enabling the Kenyan economy tap the immense potential for economic growth in the SME sector. However, the said policy framework does not emphasize on strategic relationships within firms and especially in the private sector. It is expected therefore that the conclusions of this study will shed more light around the strategy of franchise subcontracting and that possibly, the findings will be adopted to enhance the existing policy on sustainability of SMEs in Kenya.

Secondly, existing theories and especially on the strategy of Franchising seem to miss out on important issues with the evolvement of Franchising in the developing economies. Indeed, the most conspicuous aspect is that most of them seem to be out of context as far as developing economies are concerned. In drawing conclusions on the strategy of Franchise subcontracting in the selected counties in Kenya, this study is likely to highlight inconsistencies with existing theories hence identifying opportunities for further proposition of modern theories taking into consideration context factors.

Thirdly, this study will add value to practice in that its findings could be used by business entrepreneurs looking for investment opportunities to invest sustainably. The objective number one of every sensible investor is to do gainful and sustainable business. The findings of this study will add to the existing information on the strategy of Franchising and how entrepreneurs operating within the strategy have benefited in keeping their businesses sustainable or otherwise. Any new entrepreneur who cares to undertake visibility studies in considering what business strategy to adopt for their small business will find this extra piece for review. In doing so, local entrepreneurs will be able to avoid pitfalls where others have lost their investments.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

This chapter reviews the available related literature. The review will investigate the theoretical framework on franchising, franchise subcontracting as a strategy and the sustainability of SMEs. In reviewing the theoretical foundations of franchising, the study will discuss theories proposed by scholars in explaining the ‘why’ of franchising. The review on Franchising as a strategy will try to bring out the uniqueness of such manner of doing business and what other studies have said concerning such qualifying characteristics of the franchise model. The literature on sustainability of SMEs will be reviewed with keen focus in establishing the status of the statistical magnitude of the SME sustainability problem to indicate why a strategic solution is required.

#### **2.2 Theoretical Foundation**

Franchising has widely been explained as anchoring on two major theories:- The resource scarcity theory (Oxenfeldt and Kelly, 1996) and the Agency theory (Eisenhardt, 1989; Jensen & Meckling, 1976). The proponents of these theories looked at franchising from the perspective of the franchisor problem and thus most research after these theories has concentrated in explaining how the franchisor solves her problems by establishing linkages through which business risks are spread to third parties in most cases SMEs.

##### **2.2.1 Resource Scarcity theory**

Oxenfeldt and Kelly (1969) proposed that firms franchise in order to access scarce resources, particularly financial and managerial (i.e., local decision-making and market knowledge) resources, in order to expand rapidly. When franchisor firms are very young and small, it is difficult to raise adequate capital for growth through traditional financial markets (e.g., through public stock offerings) or from existing operations, and it is difficult to develop the requisite managerial talent and local market knowledge (Katz & Owen, 1992). Thus, franchisors seek to access the capital and managerial resources that franchisees provide when they build and manage outlets, even though returns might be higher among firm-owned

outlets (Oxenfeldt & Kelly,1969). In short, in the resource scarcity model proposed by Oxenfeldt and Kelly (1969), firms turn to franchising when the need to achieve economies of scale pressures them to expand at a rate beyond what is possible using only internally generated resources.

The proposal by Oxenfeldt & Kelly is within the context arguably right. Firms struggling in business with financial difficulties could use franchising as a way of borrowing from franchisees who invest in the business and offload the franchisor some costs which she would have to spend in getting the product to the consumer far and wide. By replicating a tested model in different places, the Franchisor is able to reach millions of consumers by riding on the franchisees investment. By looking at this theory from the franchisor side, it would then appear that the franchisee has unlimited resources to invest which may not be necessarily the case, however, the fact that the franchisor spreads his business to many smaller investors is what builds a resource base for her. Clearly, the resource scarcity theory as proposed by Oxenfeldt and Kelly does not focus on the franchisee or the subcontractor further down the supply chain and assumes that franchisees have got greater financial abilities than the franchisor which is not necessarily the case.

### **2.2.2 Agency Theory**

An agency relationship exists whenever one party (the principal) delegates authority to another (the agent). Inherently however, agents are found to be self-interested and to possess goals that diverge from the principal's goals, the principal must therefore expend resources (called agency costs) to ensure that agents act in her interests (Eisenhardt, 1989; Jensen & Meckling, 1976). According to Combs et al.(2004) there are two types of agency problems: vertical and horizontal.

What captures attention in the argument around the vertical agency problem is the potential for opportunistic behavior such as shirking (reduced effort) which is two-sided what Lafontaine, 1992 calls a double sided moral hazard. Given that both parties might act opportunistically, research has focused on how franchise contracts divide tasks and residual claims to create incentives that promote efficiency and minimize opportunism. Since the agency theory is build on firm to firm interlinkages principles, it would suffice to look at look deeper into how the franchise and its agents benefit create opportunities for each other in the

relationship. One could argue that the franchisee or even a franchisee subcontractor provides an opportunity for the franchisor to concentrate on her core business. This is the basis of modern business subcontracting technically referred to as outsourcing. On the other hand, the subcontracting firm finds a business opportunity within its scale of resources to handle profitably.

The horizontal agency problem refers to the potential for franchisees to free ride on other outlets. Because all outlets operate under a shared brand name and customers transfer goodwill associated with one outlet to others (Brickley & Dark, 1987; Caves & Murphy, 1976; Gal-Or, 1995), certain investments in the brand that franchisees make have spillover benefits for other franchisees. Whereas, the horizontal agency problem leading to under investment cannot be dismissed, perhaps in the context of a developing economy like Kenya, horizontal agency can be argued as creating an industry mutual effect leading to growth and sustainability. The replica effect of goodwill created by some outlets perfection of standards supports the survival of similar outlets in the market for the franchisors products. As a result, weaker outlets are able to ride on that goodwill to stability and sustainability.

In a nutshell, resource scarcity theory views franchising as a mechanism to ease financial and managerial constraints on growth and sustainability of franchisors while Agency theory views franchising as a mechanism for improving the alignment between firm- and outlet-level incentives. In conclusion, the two theories by and large fall short in clearly establishing the mutual benefit side of the Franchisee and other sub agents on the downstream side of the supply chain.

### **2.3 Franchise subcontracting concept**

The strategy of Franchise subcontracting is gaining popularity not only in Kenya but in other developing economies. Adoption of Franchise subcontracting can by and large be seen as a response to the challenges that threaten the survival of small and medium enterprises. Literature is replete with pitfalls and bottlenecks that cause firms to fail. Franchise subcontracting is perhaps one strategy that addresses the major challenges that threaten the progressive survival of SMEs. These challenges have been widely discussed in different studies and include; SMEs financing challenges (Nurbani et.al,2010),technology and innovation (Rothwell, 1991 and ILO 2005) ,unfair competition by large firms, owner skills,

limited market information (Wahome, 2013) and supply-chain bottlenecks (Hayashi, 2005; Altenburg, 1999; Lall & Mortimore, 2000).

Studies on small business performance have dealt with growth and survival. Shane (1996) argues that franchising, as compared to other hybrid strategies, has a positive effect on network growth and survival since it overcomes managerial limits to firm growth. Lafontaine and Shaw (1998) conclude that the growth rate of a small business in a format franchising is at least commensurate with the growth rate of the economy as a whole. Thus, a small business established under a franchise subcontract and cushioned from the hostilities of free owned big firm is assured of survival in a vibrant economy.

As a strategy, franchise subcontracting creates factors with a positive impact on small business growth and sustainability which include franchisor growth orientation, franchisee start-up costs (Castrogiovanni and Justis (2002)), multi-partner franchise system start-ups, franchise system piloting, prior franchising experience of the franchisor (Stanworth et al. (2004)), lowering of royalty rates as the system ages, low initial investment, financing of franchisees (Shane et al. (2006)) and close monitoring for adherence to the original franchise practice (Szulanski and Jensen (2006)).

The typical economic logic of large-small subcontracting lies in the fact that large firms can do some things better than small ones but other things less well (Berry, 1997). One of the things that large firms can do is access market information for competitive advantage. Such information in a franchise subcontract set up is thus cascaded down to the small business owner in a way to benefit him. Franchisors also use such market information to refine their distribution operating standards. Franchise subcontract agreements provide SMEs the privilege of free market research and the burden of raw material sourcing and pricing is equally lifted by the franchisor through centralized procurement arrangements. This scenario thus offers the subcontracted SME a cool haven for sustainability.

Rothwell (1991) explains, based on the data on SMEs of UK that franchise subcontracting can be an important means of gaining access to new production technologies for many small firms and can enable firms to innovate products requiring new production techniques, without having to invest initially heavily in expensive, sophisticated production equipment. Most of



the SMEs, which are basically subcontractors for other companies, do not perform research and development in any formal sense and much of their technology is derived from their franchisors. Engaging in external technical and other linkage activities can increase the technical, market and managerial know how of the small firm and can form an important part of its overall innovatory activities leading to competitiveness (ILO, 2005).

Franchise subcontracting has been cited as perhaps one of the leading business strategies which has seen the growth of small and medium enterprises due to its characteristic structure of tested business model which assures the entrepreneur an instant brand image and customer loyalty at start up and especially for entrepreneurs who may lack business management skills. Mr. Muchiri Wahome, Chief Executive Officer of Deacons – Kenya explains that most problems in a franchise have been sorted out by the franchisor in that under this model, one is able to settle down into his business faster, as opposed to when one has to develop the brand and market it herself.

Franchisors provide a cascaded operating standard commonly referred to as distributor operating standards (DOS). The operating standards require the SME owner to keep specific type of records, maintain the business premises in a certain way, employ qualified personnel and maintain proper inventory management practices. The standards thus provide the SME owner with a business model that when complied with subdues the effects of lack of business management skills on his part hence making the business successful and sustainable.

SMEs success and sustainability in developing economies is highly constrained by poor access to markets, market information, raw materials, capital, modern technology, managerial skills, sufficient production facilities and others. Franchisor parent firms, through subcontracting systems, may provide better access to these resources (Hayashi, 2005). Inter-firm linkages between large firms and SMEs in a franchise subcontract involve coordination of the activities through continuous mutual exchange of information (Lall & Mortimore, 2000). SMEs can profit from this situation in a number of ways. Large enterprises, in addition to opening up new markets for SMEs and relieving SMEs development and marketing tasks, can be an important impetus for modernization and growth (Altenburg, 1999).

## **2.4 Sustainability of SMEs**

While sustainability in the modern context popularly refers to how large organizations undertake business while at the same time conserving environmental and social resources for the sake of future generations, generally a sustainable business is one that is robust and efficient. It appeals to customers' changing values, strengthens relationships with suppliers and positions the brand as a good corporate citizen. On the other hand sustainability refers to that ability of a business to live through difficult times and demonstrate its perpetual capabilities and more specifically in the midst of mounting competition which will be the key focus of this study.

With the spread of liberalization, capitalism and globalization of economies and the resultant challenges that have hit large business set ups, entrepreneurship continues to gain importance and popularity.(Rwigema and Venter, 2004; 2005b; Chang and Li,2006). Statistics show that there is no better way to provide a broad basis for rapid economic growth than to dramatically increase the number of active and sustainable entrepreneurs in an economy (Pretorius , van Vuuren and Nieman, 2005). Linked with entrepreneurship is the SME sector.

The importance of a dynamic SME sector to the economy has highly been acknowledged (Henning 2003). SMEs are said to be major components of most economies (Miller, Besser, Gaskill and Sapp, 2003). Despite the widely acknowledged importance of SMEs in the economy, literature is replete with statistics indicating that about 60% of business startups fail before their fourth anniversary. In Kenya statistics indicate that three out of five SMEs fail within the first nine months. ( Kiege, 1991). Numerous challenges, bottlenecks and pitfalls have been cited as to why small and medium enterprises fail. The geographical location (Wasonga jack kasole, 2008), government policies (Waweru, 2002), literacy levels of entrepreneurs (Mbuvi A.K.N, 1983) and business financing ( Wanjohi and Mugure, 2008) are widely cited reasons. Other reasons include; structural, legal as well as managerial problems, which are present in the process of economic development.

In some both developing and advanced countries, the governments for their contribution consciously promote SMEs. The intervention by governments is necessitated due to the fact that with few exceptions SMEs are incapable of solving the problems with their own resources and abilities (S. Lemma, 2001). The burden laid on SMEs by regulatory frameworks in developing countries clearly place them at a disadvantaged position and indeed, according to Hellen Otieno et al, smallness confers some inherent competitive disadvantages and that some sort of external support is warranted in order for small enterprises to reach their full potential. While the government could as well solve a number of challenges related to legal frameworks and resource mobilization for SMEs entrepreneurs, there is also the case of the business strategy that an entrepreneur decides to venture into which largely determines their success or failure. It is the emphasis of Kotey and Meredith (1997) that the specific strategies which a business adopts determine to a great extent its sustainability or failure which will be the focus of this paper.

The need to fill the gap between the establishment of SMEs and their long run success cannot be overemphasized especially in view of the numerous studies which clearly underscore that survival of SMEs is highly challenged. Generally SMEs face unique problems, which affect their growth and profitability and, hence, diminish their ability to contribute effectively to sustainable development.

Lack of planning, improper financing and poor management have been cited as the main causes of failure of small enterprises (Longenecker, et al., 2006). Fiona (2003) establishes that More often than not small and medium enterprises establish managerial strategies through trial and error mechanism. Their managerial techniques only focus on operational plans rather than strategic plans of their organization. In addition, these managerial techniques are not standard with those of other global managers. Consequently, managers of small and medium enterprises are not able to adequately handle challenges facing the enterprises. Research conducted on SMEs in Africa by Mead and Liedholm (1998) found out that on average there are more SMEs closures than expansions, with only approximately 1% of micro enterprises growing from five or less employees to ten or more.

# **CHAPTER THREE**

## **RESEARCH METHODOLOGY**

### **3.1 Introduction**

This chapter will describes the methodology used in conducting the study. This includes: The research design; target population, sampling design and procedures; research instruments for data collection; the research process; validity and reliability of the research instruments as well as data processing and analysis techniques.

### **3.2 Research Design**

This study was descriptive in nature and a survey design was applied. Nachmias and Nachmias (1996) assert that research design refers to the master plan that will be used in the study in order to answer the research questions. This study being descriptive therefore described characteristics of population being studied. According to Jackson (2009), descriptive research is used to obtain information concerning the current status of the phenomena to describe "what exists" with respect to variables or conditions in a situation.

The study was a survey which according to Kerlinger (1973) will look at large population (universe) by selecting and studying the samples from the population to discover the relative incidence, distribution and interrelations of sociological and psychological variables. A cross sectional approach was used where the investigator will obtain data from respondents through questionnaires. The study was concerned with establishing the scope of adoption of franchise subcontracting by SMEs in the selected counties. It further determined the viability of franchise subcontracting as a strategy in the sustainability of SMEs. In doing

### **3.3 Target Population of the study**

In this study the target population was about 300 SMEs operating within the franchise subcontracting strategy in the major urban centers in the selected counties. The study targeted those enterprises within the urban centers where there is concentration of such enterprises and can thus be representative of most enterprise sectors in the region. Two to three major urban centres and or towns were selected in each county.

The selected counties were majorly agricultural zones and thus the target population is expected to be homogeneous in its characteristics. This means that since most of the SMEs operated within very similar conditions and environment, the probability that most traders experience common phenomenon in business is high hence generalization of findings was possible.

### **3.4 Sampling**

This study used the stratified random sampling technique. Stratified random sampling is a modification of random sampling in which the population is divided into two or more relevant and significant strata based on one or more attributes (Saunders, et. al., 2007). This sampling method was used because it is deemed suitable for a highly concentrated geographical area where face to face contact is required and also where the population can be divided into two or more sub units based on certain internal characteristics. (Mugenda and Mugenda, 1999). Each of the stratum to which the population is divided obtains an equal chance of being sampled. In this study the considered characteristic was the size of the enterprise for purposes of stratifying.

Small and medium enterprises as the name suggests fall within a range of different sizes. Research has shown that the characteristics of a population or phenomenon could be affected by for example the size of the business enterprise in this case. This study was therefore stratify the target population into different sizes based on capital investment. Proportionate stratified sampling was applied for all the strata. The advantage of stratified sampling is said to be its ability to ensure inclusion of subgroups, which would otherwise be omitted entirely by other sampling methods because of their small number in the population. Sekaran (2003) recommends that a sample size of more than 30 and less than 500 is appropriate for any social science research. Out of the estimated population of 300 SMEs, this study used a sample of 100 SMEs which is 33% of the population.

### **3.5 Data Collection**

Data was collected through structured questionnaires. The target respondents was the business owners of the sampled enterprises or the top manager in the enterprise where the owner of the business may not be available to respond. The questionnaires was administered by well-

trained research assistants to enable good coverage of the sample of interest within the vast geographical scope and circumvent time constraint. Relevant authorization was sought from the University of Nairobi and other relevant stakeholders for ethical considerations .Fifteen (15) respondents were interviewed in a pilot study. The data was then analyzed and results interpreted for correctness of the research instruments. Appropriate modification was then be done on the instruments.

The research instruments testing was aimed at ensuring that the final instruments have clear and well understood by the respondents. If the instruments are not easily understood, there is a likelihood that the respondents may give answers for the sake of it. In other cases, the respondents may choose not to respond to the questionnaire altogether hence a high rate on non-responses. The research instruments modification was then be followed by final data collection which was done by administering questionnaires and guided interviews to entrepreneurs in the strata. Observation was done throughout the period of data collection. The study used questionnaires and key informant interviews as the main tools for collecting data. Questionnaires were the most appropriate for this study as they are like

### **3.6 Data Analysis**

The data was analyzed using a statistical package for social scientist (SPSS) version 11.0 to increase the accuracy of the results. The data to be obtained from this study was numeric form hence qualitative. It was based on the experiences of the individual participants. The qualitative data was analyzed manually by first summarizing the information gathered followed by categorization and coding into emerging themes.

Qualitative analysis was the most appropriate in this study because according to (Coolican, 1994) qualitative analysis is often less influenced than is quantitative analysis by the biases and theoretical assumptions of the investigator. In addition, it offers the prospect of understanding the participants in a study as rounded individuals in a social context. This contrasts with quantitative analysis, in which the focus is often on rather narrow aspects of behavior.

## CHAPTER FOUR

### DATA ANALYSIS RESULTS AND DISCUSSION

#### 4.1 Introduction

This chapter presents the findings of the study as well as discussion of the results of the study. The findings include the background information, adoption of franchising subcontracting and sustainability of franchise subcontracting as a strategy.

#### 4.2 Response rate

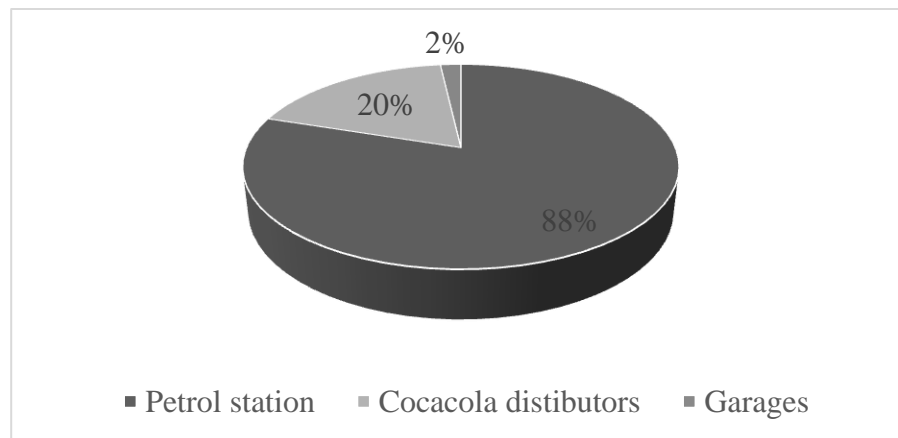
Out of 100 questionnaires distributed to SME business managers, 94 were returned fully filled and fit for analysis. This represents a 94% response rate which is above the 70% threshold recommended by Mugenda and Mugenda (2012).

#### 4.3 Background information

This section presents findings on type of business, business ownership, respondents' position in the business and the startup capital.

##### 4.3.1 Type of business

A significant number (88%) of businesses in the study were Coca-Cola distributors whereas 20% were garages.



**Figure 0.1 Type of business**

**Source: Field Data (2015)**

### 4.3.2 Business ownership

Findings in Table 4.1 shows that 47% of the SMEs in the study were limited companies while 37% were sole proprietorships.

**Table 0.1 Business ownership**

Ownership	Frequency	Percentage
Sole proprietor	35	37%
Partnership	10	11%
Limited company	44	47%
Co-operative	5	5%
Total	94	100%

**Source: Field Data (2015)**

### 4.3.3 Respondent's position in the business

Majority (63%) of the participants in the study were managers of the businesses in question, 24% were the owners of the establishments and 10% were shareholders in the business.

**Table 0.2 Respondent's position in the business**

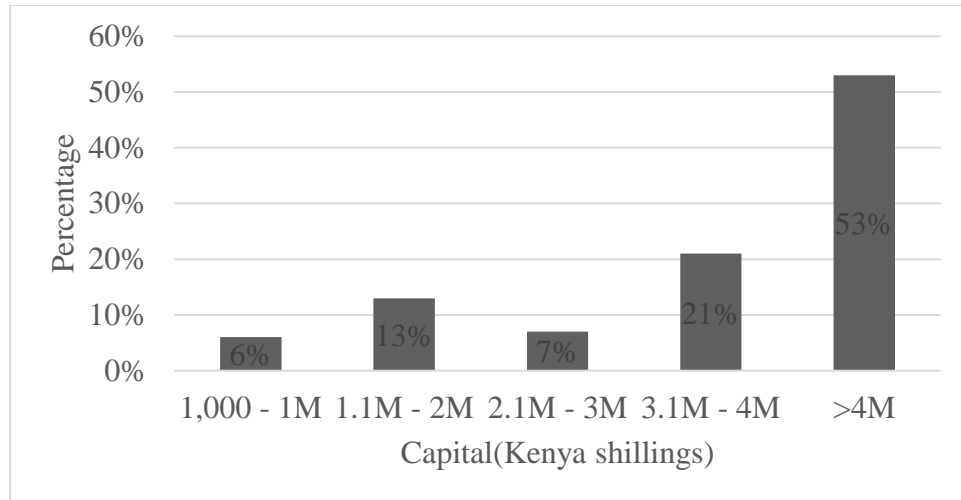
Position	Frequency	Percentage
Owner	23	24%
Partner	3	3%
Shareholder	9	10%
Manager	59	63%
Total	94	100%

**Source: Field Data (2015)**



#### 4.3.4 Startup capital

Majority (53%) of the SMEs in the study had a startup capital of over 4 million Kenya shillings. Twenty one percent had a startup capital of between 3.1 and 4 million Kenya shillings while 13% had startup capital of between 1.1 and 2 million Kenya shillings.



**Figure 0.2 Startup capital**

**Source: Field Data (2015)**

#### 4.4 Adoption of franchising subcontracting

The study sought to determine the extent of adoption of franchise subcontracting as a strategy by SMEs in the selected counties

##### 4.4.1 Business inception

Majority (66%) of the SMEs in the study were started after 2000. This shows that most of the small businesses in Nyeri were relatively young having been in operation for less than 15 years.

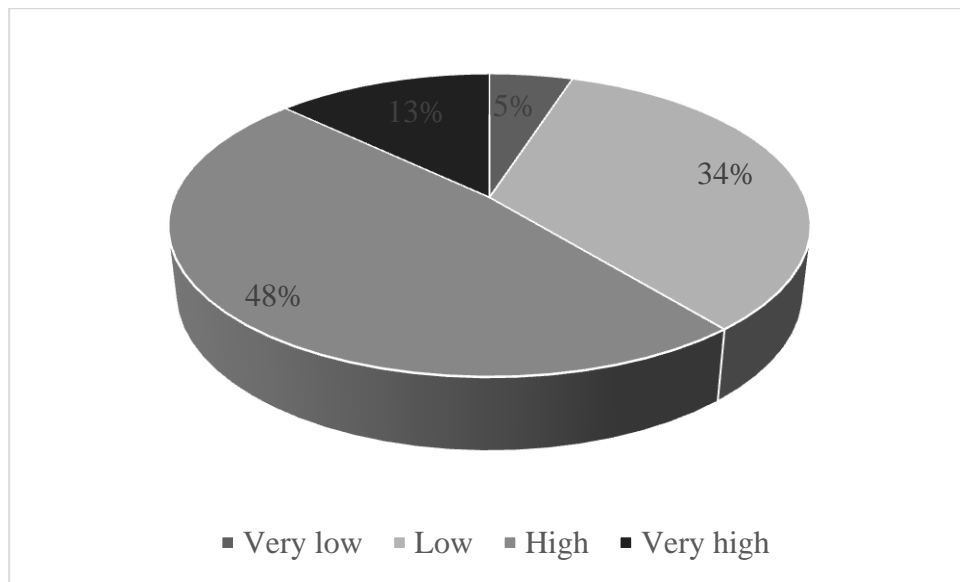
**Table 0.3 Business inception**

Year	Frequency	Percentage
Before 1970	8	9%
1971-1980	6	7%
1981-1990	5	4%
1991-2000	13	14%
After 2000	60	66%
Total	92	100%

**Source: Field Data (2015)**

#### 4.4.2 Awareness of franchise subcontracting

Findings in Figure 4.3 show that majority (61%) of the participants rated high the awareness of business men on subcontracting as a business strategy. This is in disagreement with Okatch et.al (2011) who indicated that the franchise business model has been slow to take hold in Kenya because local investors know little or nothing about its potential rewards.



**Figure 0.3 Awareness of franchise subcontracting**

**Source: Field Data (2015)**

#### 4.4.2 Target of franchise subcontracting

Majority (59%) of the participants agreed that the strategy of franchise subcontracting targets businesses across all industries in Nyeri County.

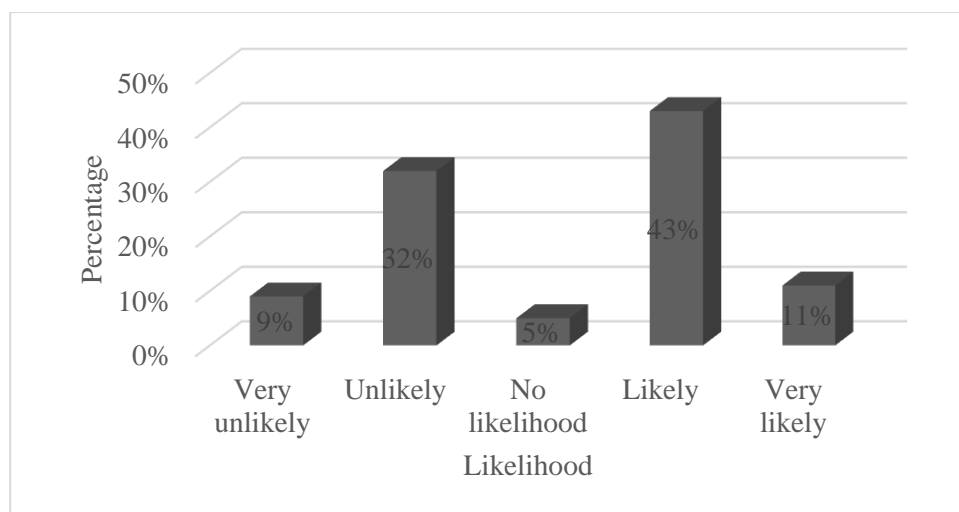
**Table 0.4 Target of franchise subcontracting**

Response	Frequency	Percentage
Disagree	19	20%
I have no idea	19	20%
Agree	54	57%
Strongly agree	2	2%
Total	94	100%

**Source: Field Data (2015)**

#### 4.4.3 Likelihood of more businesses operating under franchise subcontracting

Majority (54%) of the respondents indicated that it was highly likely that more businesses operated under franchise subcontracting strategy than freelance businesses.

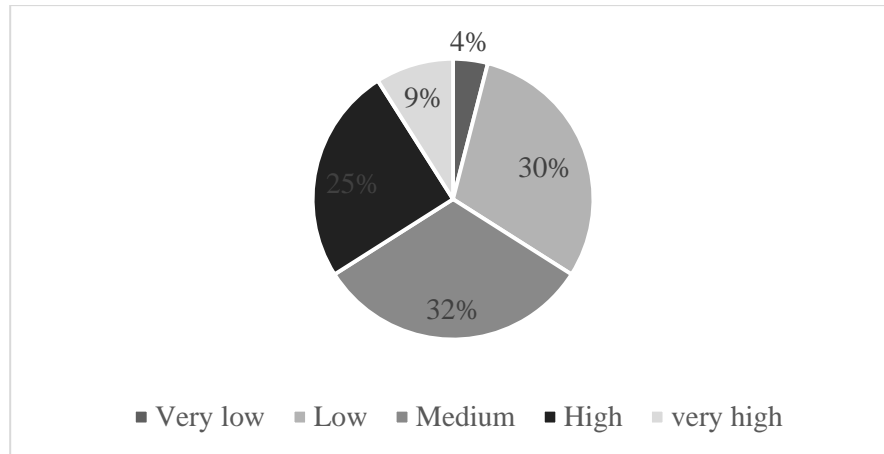


**Figure 0.4 Likelihood of more businesses operating under franchise subcontracting**

**Source: Field Data (2015)**

#### 4.4.4 Likelihood of new businesses operating under franchise subcontracting

Findings in Figure 4.5 show that 34% rated high while 32% of the respondents rated medium, the likelihood that more small and medium business men will start new businesses within a franchise subcontracting agreement in the following two years.



**Figure 0.5 Likelihood of new businesses operating under franchise subcontracting**

Source: Field Data (2015)

#### 4.4.5 Number of new businesses operating franchise arrangement

Seventy three percent of the respondents indicated that the number of new small and medium businesses operating under a franchise subcontract arrangement was increasing in the previous two years.

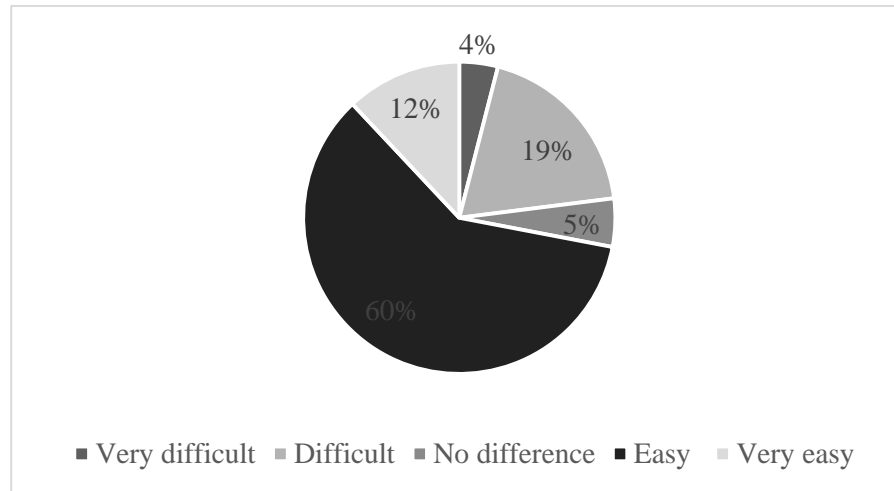
**Table 0.5 Number of new businesses operating franchise arrangement**

Response	Frequency	Percentage
Highly declining	1	1%
Declining	7	7%
No Idea	17	18%
Increasing	67	71%
Highly increasing	2	2%
Total	94	100%

Source: Field Data (2015)

#### 4.4.6 Market penetration of businesses under franchise subcontract

Majority (72%) of the participants indicate that it was very easy for a business under a franchise subcontract arrangement to penetrate the market as opposed to a freelance business.



**Figure 0.6 Market penetration of businesses under franchise subcontract**

**Source: Field Data (2015)**

#### 4.5 Sustainability of franchise subcontracting as a strategy

The study sought to determine the viability of franchise subcontracting strategy in the sustainability of small and medium enterprises.

##### 4.5.1 Competitive advantage of businesses operating on franchise subcontracting

Seventy one percent of the respondents agreed that small and medium businesses operating under franchise subcontracting enjoyed competitive advantage over their freelance competitors. This finding is in agreement with Oxenfeldt and Kelly (1969) who indicated that firms struggling in business with financial difficulties could use franchising as a way of borrowing from franchisees who invest in the business and offload the franchisor some costs which she would have to spend in getting the product to the consumer far and wide

**Table 0.6 Competitive advantage of businesses operating franchise subcontracting**

Response	Frequency	Percentage
Strongly disagree	6	6%
Disagree	13	14%
I have no idea	8	9%
Agree	63	67%
Strongly agree	4	4%
Total	94	100%

**Source: Field Data (2015)**

#### **4.5.2 Survival of businesses operating franchise subcontracting**

Majority (60%) of the participants indicated that often, most small and medium businesses operating under franchise subcontracting agreements were known to have survived the lifetime of their owners. This is in agreement with Nurbani et al. (2010) adoption of Franchise subcontracting can by and large be seen as a response to the challenges that threaten the survival of small and medium enterprises

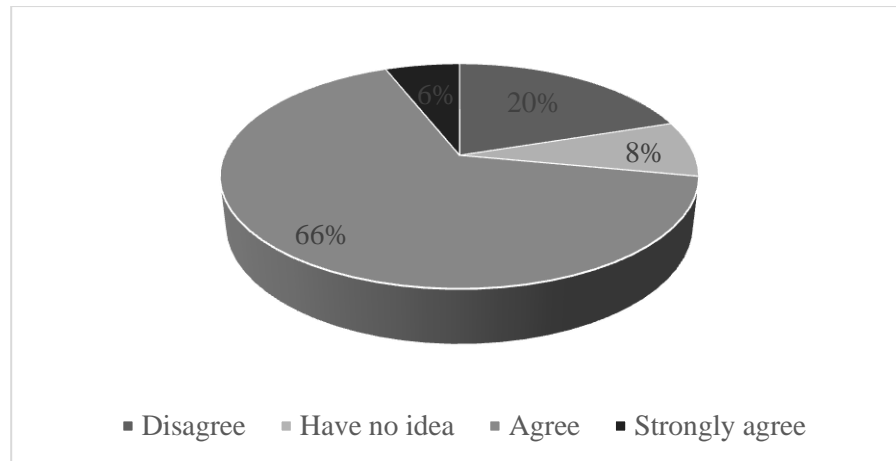
**Table 0.7 Survival of businesses operating franchise subcontracting**

Response	Frequency	Percentage
Very rarely	3	3%
Rarely	20	21%
Hard to tell	15	16%
Often	37	40%
Very often	19	20%
Total	94	100%

**Source: Field Data (2015)**

### 4.5.3 Marketing support and supervision

Seventy two percent of the respondents agreed that the marketing support and supervision by the subcontracting franchise and franchisor enables small and medium businessmen survive hard times regardless of their level of education. This finding is consistent with Berry (1997) who indicated that one of the things that large firms can do is access market information for competitive advantage. The findings are also in agreement with ILO (1997) who found that most of the SMEs, which are basically subcontractors for other companies, do not perform research and development in any formal sense and much of their technology is derived from their franchisors.



**Figure 0.7 Marketing support and supervision**

**Source: Field Data (2015)**

### 4.5.4 Profitability of small and medium businesses

Half (50%) of the respondents agreed that small and medium businesses were profitable since they were protected from competition from the same product brand by way of market territory demarcation. However, 32% of the respondents disagreed and 16% indicate that they had no idea. The findings are consistent with Lafontaine and Shaw (1998) who concluded that the growth rate of a small business in a format franchising is at least commensurate with the growth rate of the economy as a whole.

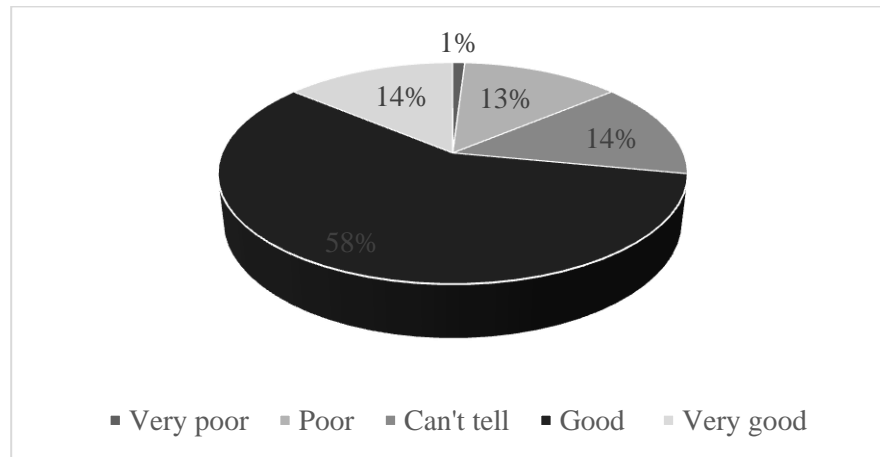
**Table 0.8 Profitability of small and medium businesses**

Response	Frequency	Percentage
Strongly disagree	2	2%
Disagree	30	32%
I have no idea	15	16%
Agree	36	38%
Strongly agree	11	12%
Total	94	100%

**Source: Field Data (2015)**

#### 4.5.5 Profitability of franchise businesses

Sixty two percent of the respondents rated well the profitability of their businesses in comparison to similar business operating outside the franchise arrangement. This is in agreement with Shane (1996) who argued that franchising, as compared to other hybrid strategies, has a positive effect on network growth and survival since it overcomes managerial limits to firm growth



**Figure 0.8 Profitability of franchise businesses**

**Source: Field Data (2015)**



#### 4.5.6 Contribution of franchising to business success

Majority (77%) of the respondents indicated that to a high extent, they attributed their business success to the fact that they were operating under the strategy of franchise subcontracting as opposed to other factors. This is in agreement with Castrogiovanni and Justis (2002) who observed that franchise subcontracting creates factors with a positive impact on small business growth and sustainability which include franchisor growth orientation, franchisee start-up costs.

**Table 0.9 Contribution of franchising to business success**

Response	Frequency	Percentage
Very Low extent	2	2%
Low extent	13	14%
No extent	6	6%
High extent	71	75%
Very high extent	2	2%
Total	94	100%

**Source: Field Data (2015)**

#### 4.5.7 Likelihood of converting to freelance model

Seventy three percent of the participants indicated that they had a very low urge to quit their current business model in favor of a freelance model.

**Table 0.10 Likelihood of converting to freelance model**

Response	Frequency	Percentage
None	6	6%
Very low	22	23%
Low	47	50%
High	6	7%
Very high	13	14%
Total	94	100%

**Source: Field Data (2015)**

#### 4.5.8 Likelihood of business surviving its 20th anniversary

Majority (74%) indicated that there was a very high likelihood that the business they were operating then would survive its 20<sup>th</sup> anniversary. This is consistent with Lafontaine and Shaw (1998) who indicated that a small business established under a franchise subcontract and cushioned from the hostilities of free owned big firm is assured of survival in a vibrant economy.

**Table 0.11 Likelihood of business surviving its 20th anniversary**

Response	Frequency	Percentage
Very low	3	3%
Moderate	21	22%
High	53	56%
Very high	17	18%
Total	94	100%

**Source: Field Data (2015)**

#### 4.5.9 Effect of franchising on sustainability

Respondents in the study were asked to rate the extent to which various elements of franchising affected the sustainability of their business. Findings are presented in Table 4.12. Majority (68%) indicated that tested business format and protection from unfair competition by same product brand through territory demarcation and control of new entrants affected the sustainability of their business (mean =2.28). This is in agreement with ILO (2005) who indicated that franchising leads to growth of small and medium enterprises due to its characteristic structure of tested business model which assures the entrepreneur an instant brand image and customer Delivery of products free of charge to your business premises was rated as not applicable by majority (53%) of participants (mean=2.80). Product advertisement by the franchisor in public media was rated highly by 66% (mean=2.3). Similarly, marketing support by the franchisor in operational strategies and promotions was rate highly by 68% (mean=2.32). This finding is consistent with Berry (1997) who indicated that one of the things that large firms can do is access market information for competitive advantage. Such

information in a franchise subcontract set up is thus cascaded down to the small business owner in a way to benefit him.

Sixty eight percent of the respondents highly rated retail price recommendation execution support and supervision by franchisor (mean=1.01). Forty eight percent highly rated support by the franchisor through provision of free marketing equipment, however, 25% indicated that this was not applicable (mean=2.19). Majority (60%) rated training/coaching on business model success strategies by the franchisor staff (mean=2.36). Performance management by the franchisor through monthly target setting was also rated highly by 80% of the respondents (mean=1.91). Majority (59%) highly rated regular incentives by the franchisor on achievement of targets (mean=2.53). The findings are in agreement with Berry (1997) who found that franchise subcontract agreements provide SMEs the privilege of free market research and the burden of raw material sourcing and pricing is equally lifted by the franchisor through centralized procurement arrangements.

**Table 0.12 Effect of franchising on sustainability**

Franchise characteristic	Very large extent	Large extent	Not applicable	Small extent	Very small extent	Mean	SD
Tested business format and protection from unfair competition by same product brand through territory demarcation and control of new entrants	23%	45%	13%	19%		2.28	1.03
Delivery of products free of charge to your business premises	17%	13%	53%	7%	10%	2.80	1.11
Product advertisement by the franchisor in public media	25%	41%	16%	16%	2%	2.3	1.09
Marketing support by the franchisor in operational strategies and promotions	28%	40%	12%	11%	9%	2.32	1.23
Retail price recommendation execution support and supervision by franchisor	28%	40%	17%	15%		2.19	1.01
Support by the franchisor through provision of free marketing equipment	16%	32%	25%	23%	4%	2.68	1.13
Training/coaching on business model success strategies by the franchisor staff	28%	32%	18%	21%	1%	2.36	1.14
Performance management by the franchisor through monthly target setting	36%	44%	13%	7%		1.91	0.9
Regular incentives by the franchisor on achievement of targets	18%	41%	15%	23%	3%	2.53	1.13

**Source: Field Data (2015)**

## **CHAPTER FIVE**

### **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Introduction**

This chapter presents a summary of the findings as presented in the previous chapter. In addition, the study's conclusion and recommendations are also presented.

#### **5.2 Summary**

##### **5.2.1 Adoption of franchising subcontracting**

The first objective of this study sought to determine the extent of adoption of franchise subcontracting as a strategy by SMEs in the selected counties. The study found that majority (61%) of the participants rated high the awareness of business men on subcontracting as a business strategy. Majority (54%) of the respondents indicated that it was highly likely that more businesses operated under franchise subcontracting strategy than freelance businesses. Seventy three percent of the respondents indicated that the number of new small and medium businesses operating under a franchise subcontract arrangement was increasing in the previous two years. 34% rated high while 32% of the respondents rated medium, the likelihood that more small and medium business men will start new businesses within a franchise subcontracting agreement in the following two years. Majority (72%) of the participants indicate that it was very easy for a business under a franchise subcontract arrangement to penetrate the market as opposed to a freelance business.

##### **5.2.2 Sustainability of franchise subcontracting as a strategy**

The second objective of the study sought to determine the viability of franchise subcontracting a strategy in the sustainability of small and medium enterprises. Seventy one percent of the respondents agreed that small and medium businesses operating under franchise subcontracting enjoyed competitive advantage over their freelance competitors. Majority (60%) of the participants indicated that often, most small and medium businesses operating under franchise subcontracting agreements were known to have survived the lifetime of their owners. Seventy two percent of the respondents agreed that the marketing support and

supervision by the subcontracting franchise and franchisor enables small and medium businessmen survive hard times regardless of their level of education.

Half (50%) of the respondents agreed that small and medium businesses were profitable since they were protected from competition from the same product brand by way of market territory demarcation. Sixty two percent of the respondents rated good the profitability of their businesses in comparison to similar business operating outside the franchise arrangement. Majority (77%) of the respondents indicated that to a high extent, they attributed their business success to the fact that they were operating under the strategy of franchise subcontracting as opposed to other factors. Seventy three percent of the participants indicated that they had a very low urge to quit their current business model in favor of a freelance model. Majority (74%) indicated that there was a very high likelihood that the business they were operating then would survive its 20th anniversary.

### **5.3 Conclusion**

The study concludes that adoption of franchising subcontracting strategy is gaining high adoption among small and medium enterprises in the market. The findings of this study suggest that the number of new small and medium businesses operating under a franchise subcontract arrangement was increasing in the previous two years prior to the study and there was a high likelihood that more small and medium business men will start new businesses within a franchise subcontracting agreement in the following two years. The researcher attributes the increased adoption of this strategy to increased awareness of the benefits of franchising among small business owners.

The study concludes that sustainability of SMEs operating under franchise subcontracting strategy is high. The findings of the study suggest that apart from gaining competitive advantage and increasing profitability, most small and medium businesses operating under franchise subcontracting agreements were known to have survived the lifetime of their owners. In addition there was a very high likelihood that the business they were operating then would survive its 20th anniversary. The researcher attributes the high survival and therefore sustainability of SMEs operating under the franchise model on prior franchising experience of the franchisor, low initial investment, financing of franchisees and close monitoring for adherence to the original franchise practice. These benefits of franchising

shield SMEs from market challenges such as competition, access to credit and lack of market information thereby increasing their profitability and ultimately ensuring their survival.

#### **5.4 Recommendations and implications on policy, practice and theory**

More SMEs should adopt the franchise subcontracting strategy to increase successful entry, SME sustainability and profitability. This is because the number SMEs currently operating franchises in Nyeri, Laikipia, Embu and Meru Counties is low compared to the total number of SMEs in the counties. County governments, non-governmental organizations and the Kenya National Chamber of commerce should organize training seminars for small businesses owners to enlighten them on the franchise strategy. Furthermore, the authorities can use this study to enhance their economic development policies by adopting and supporting franchise subcontracting for SMEs in their areas of jurisdiction. This study will also go a long way in enriching theory and available literature on the franchise business strategy for review and further research by other scholars.

#### **5.5 Limitations of the study**

The study focused only on adoption and sustainability of the franchise subcontracting strategy. Many other important aspects of the franchise subcontracting strategy were left out including the challenges faced by SMEs franchise subcontractors due to the conditions imposed by the franchise agreements. Furthermore, one would be interested in understanding the reasons why the franchise subcontracting strategy has taken so long to gain popularity despite having been introduced in the country several decades ago.

Most of the responded were reluctant in filling the questionnaire. The researcher handled this problem by carrying an introduction letter from the University of Nairobi and assured the respondents that the information they gave would be treated with confidentiality and was used purely for academic purposes.

The study was also limited by the financial and time constraints. The period over which the study was to be conducted was short, hence exhaustive and therefore comprehensive research could not be undertaken on the adoption and sustainability issues surrounding the franchise subcontracting strategy.

Whereas the researcher selected three industries perceived to have established SMEs operating under the franchise subcontracting strategy, the motor vehicle dealership turned out to have very few SMEs operating under the said strategy in the selected counties hence becoming a fairly low representative stratum in the research.

### **5.6 Sugestions for further study**

The current study found that despite the increasing awareness about franchise subcontracting and similarly increased adoption of the strategy by SMEs, the number of such SMEs operating under the franchise subcontracting strategy was still very low in comparison with their counter - parts operating in freelance. More research should therefore go into finding out why despite the high number of SMEs in the country, franchising subcontracting was still low. The studies could particularly investigate the perceptions commonly held about the conditions contained in a franchise agreement and their effect on rapid adoption of the franchise subcontracting strategy y in the country. Furthermore, investigations into why the franchise subcontracting strategy has taken several decades to become popular in Kenya should be carried out



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## APPENDICES

### APPENDIX I : LETTER OF INTRODUCTION

Dear Respondent,

My name is Timothy Muthini. I am a student at the University of Nairobi undertaking a degree in Master of Business Administration (Strategic Management). I am undertaking a research project entitled: **Franchise subcontracting as a strategy for sustainability of SMEs in the Mount Kenya region.**

You have been selected to participate in this study to obtain your perceptions and views regarding various aspects of franchising subcontracting in the SME sector. There wrong answers but your honest participation in answering the questions will assist in establishing the the viability of Franchise subcontracting strategy for SMEs. The information provided will be treated with strict confidentiality.

Thank you in advance.

**Timothy M. Muthini**

**MBA student**

**University of Nairobi**

**Date.....**

## APPENDIX II: RESEARCH QUESTIONNAIRE

### SECTION A – BACKGROUND INFORMATION

1. Name of business (SME) .....
2. Location ( Town / Shopping centre).....
3. Type of business ( Activity).....
4. Industry .....
5. Business ownership  
Sole proprietor   Partnership   Limited Company   Co-operative.
6. Start up capital ;  
1000 - 200,000    200,000 - 500,000    500,000- 1 million    2m and above.  
 Inherited.

### SECTION B – ADOPTION OF FRANCHISING SUBCONTRACTING

*(Instructions: Please tick the answer that best describes your opinion)*

7. What would you say is your level of understanding of the strategy of franchise subcontracting?  
Fair    fairly good   good   very good   Excellent
8. What level of awareness do you think entrepreneurs in this town have about franchise subcontracting as a business strategy?  
None    Very low   Low    High    very high.

9. The strategy of franchise subcontracting targets businesses across all industries in this county.

I strongly disagree    I disagree    I have no idea    I agree    I strongly agree

10. How many entrepreneurs operating within a franchise agreement do you know in this town.

less than 5    6 - 10    11-15    16-20    More than 20.

11. What is the likelihood that more entrepreneurs will to adopt the strategy of franchise subcontracting for their businesses in future in this town?

Very unlikely    Unlikely    I cant tell    Likely    Very likely

12. What can you say is the trend of adoption of the strategy of franchise subcontracting by small and medium enterprises in this ?

Highly declining    Declining    Constant    Increasing    Highly increasing

### **SECTION C: VIABILITY OF FRANCHISE SUBCONTRACTING AS A STRATEGY**

*(Instruction: Please tick the option that best represents your opinion.)*

13. The strategy of franchise subcontracting supports sustainability of small and medium enterprises.

I strongly disagree    I disagree    I dont know    I agree    I strongly agree

14. The strategy of franchise subcontracting is preferable for small and medium enterprises than a free ownership model?

I strongly disagree    I disagree    I dont know    I agree    I strongly agree

15. The strategy of franchise subcontracting assures small businesses survival against competition in this town?

I strongly disagree    I disagree    I cant tell    I agree    I strongly agree

16. Most small businesses operating in this town within the strategy of franchise subcontracting have been operating for more than 5 years.

I strongly disagree    I disagree    I cant tell    I agree    I strongly agree

17. On average how much would you estimate your profit to be as a percentage of monthly sales.

Below 10%    10% – 15%    16% - 20%    21% - 25%    Above 25%

18. To what extent would you attribute your business success to the fact that you are operating under the strategy of franchise subcontract as opposed to if it was a free - owned small business?

Less than 20%    20%- 40%    40%- 60%    60%-80%    More than 80%