Micro-Franchising: a viable and sustainable business model for the Swiss Development Cooperation Agency?

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Abstract

The popularity of the micro-franchising theory among practitioners in the world of international development as a development tool is steadily increasing. Through the promotion of sustainable forms of entrepreneurship at the bottom of the pyramid (BOP), it is seen as a functioning development tool that could lift people out of poverty.

This assessment report for the Swiss Agency for Development and Cooperation (SDC) aims at highlighting the benefits and limitations of the micro-franchising business model as a tool in the fight against poverty, bearing in mind that the whole concept lacks, due to its recent development, a profound theoretical framework.

Building on a literature review of the (micro-) franchising theory, this paper analyses the current best practice (18 different micro-franchising projects) and uses the findings in order to provide the SDC with some food for thoughts (through two ongoing initiatives that are potentially suited to be scaled up using micro-franchising).

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Introduction

Over the past 15 years, micro-franchising has been enjoying an ever increasing popularity amongst practitioners in the world of international development. Arguing that the approach enables one to leverage the basic concepts of traditional franchising, advocates such as Gibson (2007) and Fairbourne (2007), depict micro-franchising as a development tool which notably succeeds in promoting sustainable forms of entrepreneurship at the bottom of the pyramid (BOP), thereby lifting people out of poverty. Despite of this, it must be stated that as of now, the concept lacks a profound theoretical framework as current literature is almost exclusively based on case study analysis and case reports.

This assessment report for the Swiss Agency for Development and Cooperation (SDC) aims at highlighting the benefits and limitations of the micro-franchising business model as a tool in the fight against poverty. The SDC is currently investigating the potential of micro-franchising as a solution for the distribution of poverty alleviating products and services amongst those most in need. As such this report will focus on the applicability of micro-franchising as distribution model for such products and services.

In order to do so, we start by examining the implicit theoretical assumptions underlying the approach by briefly reviewing the current literature on franchising as well as micro-franchising. Despite of differing underlying motivations, we believe that starting by considering the traditional franchising literature is particularly useful for our purposes, seeing as this enables us to build upon a more established academic tradition. While the micro-franchise literature addresses specific issues, which typically arise due to challenging contexts in which such projects are implemented, the traditional literature provides a more compelling account of how internal dynamics between concerned actors play out. Having derived the respective theoretical imperatives which need to be taken into consideration when designing a micro-franchise project, we pursue by considering actual best practices. We close our discussion by assessing the potential for scaling-up of two existing SDC projects using a micro-franchising business model.

1. Theory of Franchising

The aim of this section is to consider the findings made by the franchising literature, which are relevant for our analysis of the potential use of micro-franchising as a tool for the SDC. As such, we start by examining what defines franchising. We then address the question of what motivates businesses to franchise, before finally considering the impact franchising has had in developing countries.

1.1. Definition

Franchising does not fit comfortably within the bounds of any single academic discipline or area of management studies: marketing, law, economics, entrepreneurship, human resources, organizational theory, sociology – these are only some of the numerous fields in which franchising falls in. As such, it should not come as a surprise that there hardly exists a universal definition of what franchising is. Despite of this conceptual fuzziness, one finds that franchising is typically considered as a strategy for firm expansion. The *Deutscher Franchise Verband*[1] [DFV] (2014) states:

> *"Franchising ist ein auf Partnerschaft basierendes Vertriebssystem mit dem Ziel der Verkaufsförderung."*

When discussing the alternatives to franchising, the International Franchise Association [IFA] (2014a) states:

> *"(..) other popular methods by which businesses expand their market and distribution channels (…)"*

Franchising consists of two legally independent parties entering in a relationship which entails, a person or a group of people (franchisee), acquiring the right to sell or produce a product or a service using the corporate identity and/or technological know-how of another business (franchisor), in exchange of some form of monetary compensation (IFA, 2014b).

While the specifics of franchise-contracts vary greatly, the franchisor typically provides the franchisee with marketing assistance, support in assuring start-up funding, bulk purchasing,

[1] German Franchising Association

constant product development, ongoing training and guidance, pre-determined operational procedures and practices, as well as the rights to use an established brand name. The franchisee on the other hand is typically required to pay franchising fees either in the form of royalties or a percentage of revenues. Furthermore he commits to a given standard of quality in product/service production/distribution, while pursuing the greater good for a given franchise concept by bringing various inputs – be they in the form of financial or human capital – to the table (Henriques & Nelson, 1997, p. 24).

As has already been alluded to previously, one typically distinguishes between two types of franchising arrangements: product distribution and business format franchises. In the first case, the franchisor licenses the use of its trademark and logo while remaining the sole proprietor of the technological and operational know-how necessary to run the business in question. These kinds of franchise-arrangements are typically to be found in the beverage and automotive industry. Business format franchisees however, receive not only the right to use a franchisors product/service, trademark and logo, but they also become the beneficiaries of an established business model including an established marketing plan and operations manual (IFA, 2014b).

1.2. Why do companies franchise?

When considering why companies use franchising in order to grow – as opposed to establishing a new location – one finds that the literature can be broadly divided into two different approaches which consider different motivations driving franchising: resource scarcity and agency considerations.

Resource Scarcity

Starting with the premise that large chains possess substantial scale advantages, early theorists of franchising have described it as method through which small or young businesses can incorporate the scarce resources needed for rapid expansion (Combs et al., 2004). These can range from financial capital (Oxenfeldt & Kelly, 1969; Hunt, 1973), human capital (Norton, 1988), managerial talent (Oxenfeldt & Kelly, 1969; Combs & Castrogiovanni, 1994) to local knowledge (Combs & Castrogiovanni, 1994). It is argued that franchisors make up for the loss of a part of future revenue flows through lower capital costs as well as better results due to self-selection of particularly talented managers as well through the integration of local knowledge. A central claim arising out of the resource scarcity argument has been that as franchisors grow, they should start refraining from using franchising as a method of business expansion, seeing as they now possess sufficient disposable financial and human capital. Furthermore, one should also observe the gradual buy-back of particularly successful franchises by the franchisor, so as to increase the franchisor's profitability. As such, franchising is seen as a mean to rapidly expand in order to achieve economies of scale early on in a company's life-cycle. Once these economies of scale are achieved this process is reversed over time (Oxenfeldt & Kelly, 1969).

The resource scarcity approach however has been heavily criticized by subsequent research, which has argued that the aforementioned conception stands in conflict with finance theory. Both Rubin (1978) and Norton (1988) show that in the context of United States, it would be more efficient to sell shares of a chain while expanding rather than proceeding with franchise buybacks later on. Norton further argues that the only situation in which using franchising as a means of gaining access to more capital can be rationally justified is when franchisors are more risk-averse than franchisees. It is argued however, that this is not the case, because a franchisee typically invests the quasi-entirety of his life-savings in order to start his business, nulling his opportunity of investment diversification. As such, the franchisee demands a risk premium, resulting in the fact that his capital comes at a higher price than in the case of a passive investor (Norton, 1998). Others have found that quite to the contrary of resource scarcity predictions, firms use more rather than less franchising when they grow, while franchisee buy-backs remain a marginal phenomenon (Combs & Castrogiovanni, 1994; LaFontaine & Shaw, 1999; Brickley & Weisbach, 1991). Interestingly, one finds no outright rejection of resource scarcity arguments based on human capital, managerial talent and/or local knowledge.

Agency Theory

More recent theorists have argued that franchising is to be considered as a solution in the context of principal-agent considerations. In the presence of rational, self-interested actors, franchising is seen as solution to vertical-agency problems (Combs et al., 2004). This is achieved by the inherent nature of the franchisor-franchisee relationship, which aligns the interests of both actors through two mechanisms: firstly, the franchisee is rewarded for efficiency with a share of the ensuing profit and secondly, as an owner-manager, he personally bears the risks of running the business (Norton, 1988). Shane (1996) confirms this line of argumentation by finding that franchises exhibit lower levels of shirking. As such, it is argued that franchisors make up for the loss of a part of future revenue flows through lower monitoring costs as well as better results due to increased efficiency. A central claim is that as such, franchising should be especially wide-spread in industries characterized by high monitoring costs and repeat customers, as constant, high-quality products and service have a more direct impact on business performance. If this is not the case, horizontal agency problems arise and free-riding[2] on brand-building efforts of others are to be expected. It is argued that horizontal-agency problems are addressed by providing franchisees with quasi-rents (i.e. higher revenues than they would receive, as independent entrepreneurs), making termination of the franchising relationship an effective threat (Combs et al., 2004).

Critics of this approach have argued that agency theory ignores historical realities by assuming that franchisors necessarily expand with already established brand names and business processes, which in turn ignores the franchisee's role in creative problem-solving and his contributions to strategic decision-making (Carney & Gedajlovic, 1991). Others have further criticized agency theory for overestimating the degree to which the franchisor-franchisee relationship aligns interests, by assuming unilateral control of the former on the latter (Bergen et al., 1992; Stanworth & Dandrige, 1994).

In spite of these conceptual criticisms, empirical research appears to largely confirm the predictions made by the proponents of agency theory. Norton (1988) finds that a higher incidence of monitoring cost proxies – population dispersion and labor intensity – translates into a higher incidence of franchise-holders. Not only do Brickley & Dark (1987) confirm the aforementioned findings, they further show that low initial investment costs per unit as well as a higher frequency of repeat customers seem to favor franchising.

Convergence of both approaches

Finally, other researchers have focused on reconciling both lies of argumentation while further considering other theoretical arguments. Martin (1988) for example has argued that franchising research needs to consider different arguments at different times of a business life-cycle. He finds that resource scarcity argument – rapid expansion in order to achieve scale-efficiencies – come to play early on in a franchise's life, while agency considerations take over as monitoring costs increase with size. Combs et al., (2004) argue along similar lines. Franchising they find, appears to influence growth and survival as predicted by resource scarcity theory. The propensity to franchise however, is determined by monitoring costs and industry type as predicted by agency theory.

[2] E.g. disregard for hygienic standards, lower-quality products, etc.

1.3. Impact of franchising in developing countries

From a development agency's perspective, it appears to be quite relevant to not only consider the impact that a given product, service or technology distributed through franchising has on a given socio-economic context, but also to consider the potential impact of using franchising as distribution mechanism.

The literature on the impact of franchising in developing countries remains in its infancy to this date. While there are a number of authors which have pursued case-studies for given country and industry contexts (e.g. Preble & Hoffman, 1995; Alon & Welsh, 2001; Siggel et al., 2003), the subject remains contentious. This is on one hand due to the fact that it relates to the general globalization debate and on the other hand because insufficient data has prevented a systematic and differentiated study of the subject at hand (Alon, 2006). Due to the inherent lack of comparability of different developing market contexts, we will refrain from attempting to list up the entirety of the literature which could potentially be relevant in this area. Nevertheless, Alon (2004) has compiled a useful list of impact evaluation criteria which are to be considered in the context of international franchising. From the Swiss Development Agency's perspective, it appears useful to evaluate on a case by case basis the potential extent to which one or the other of these socio-economic benefits and costs come to play.

Socioeconomic benefits	***Socioeconomic costs***
Output creation (direct, indirect and induced)	Output destruction due to replacement of non-franchised business
Job creation (direct, indirect and induced)	Job destruction due to replacement of non-franchised business
Tax base increase due to higher output, higher efficiency of new business and more accurate reporting	Tax base decrease due to "mom-and-pop" business and SME's not being able to compete
Economic modernization and infrastructure development	Displacement of workers employed in inefficient or outdated sectors
Economic clustering	Uneven economic development
Reduction in capital flight due to local investment	Short-term BOP deficits due to imported goods and capital outflows (royalties)
Long-term economic growth due to higher levels of entrepreneurship and SME development	Increased inequality due to emergence of new entrepreneurial class
Diffusion of innovation; increased competition resulting in lower prices and increased consumer choice; more efficient supply chains	Franchisee failure
Franchising education and skill transfer	Many jobs are menial in nature requiring a low need for skill development
Transfer of "Western" managerial expertise and business models	"McDonaldization" of society resulting in the destruction of local cultural fabric
Increase of in consumer choice	Rationalization of consumer choice
Consistent prices and quality	Prices of foreign franchisors often higher than local alternatives
	Source: adapted from Alon, 2004, p. 157

Figure 1: Impacts of International Franchising

2. Theory of Micro-Franchising

The following section focuses on the theoretical dimension of micro-franchising. First we consider what micro-franchising is and what its objectives are. We then pursue by discussing the contextual specifics and the adaptions made by micro-franchising compared to the traditional franchising business model (explained above). We conclude by stating the requirements needed to successfully micro-franchise from a theoretical perspective.

2.1. Definition

The literature on micro-franchising does not build on a differentiated theoretical basis. As a relatively recent phenomenon with the majority of micro-franchises emerging only in the last few years (Gibson, 2007: 24). Much of what we know concerning micro-franchising derives from practitioners' reports and case study analysis and as such, is not grounded in any particular theoretical framework. More specifically, no theoretical discourse exists drawing on agency and resource scarcity theories which are currently considered the standard in traditional franchising (Kistruck, et al., 2011: 506). This is the case despite of the fact that Fairbourne (2007: 8) declares the importance of learning from traditional franchising as it presents the foundation for micro-franchising. Micro-franchising is a development tool presenting itself in the form of a business model. Essentially the concept combines the business model of traditional franchising with the social connotation of "micro"; referring to poverty alleviation, benevolence, base of the pyramid and sustainability (Fairbourne, 2007: 8).

The shared prefix points to the emphasis on selected services for very low-income clients. Microcredit refers to providing very small loans to impoverished people, whereas in micro-franchise it signifies the focus on small businesses run by necessity entrepreneurs (Jones Christensen, et al., 2008: 596). Literature and practice both stress the synergic benefits deriving from completing micro-franchising by micro-financing, as often the would-be franchisee lacks the capital to become one (Hatch, 2007).

We have previously seen that firms operating in mature market economies opt for franchising business model in order to increase profits. In contrast the objective of micro-franchising is first and foremost to assist the poor by creating sustainable income through owning and operating their business and by that means, providing them with social and economic benefits (Fairbourne, 2007: 8f.) Scholars agree on entrepreneurship as being one of the key factors for economic development and thus lifting people out of poverty (Hürlimann, 2011: 3). Relevant literature stresses especially three core problems that prevent people at the bottom of the pyramid (BOP)[3] from becoming economically self-reliant (Fairbourne, 2007: 9):

1) The lack of skills needed to grow a successful business
2) The lack of jobs in developing countries
3) The lack of goods and services available to the poor

Micro-franchising offers a solution to these core problems. First by providing people who do not poses entrepreneurial skills with a business blue-print. Following this formula leads the franchisee to greater individual economic success, without even requiring an entrepreneurial spirit. Second, micro-franchises are often larger than traditional microenterprises, thus creating jobs also for those who are better suited as employee as they lack managerial skills. And third, multinational corporations (MNCs) gain through micro-franchising an effective method to deliver their goods and services to the BOP at an equitable price (Fairbourne, 2007: 9). This again allows consumers to increased access to goods, services and a higher quality of life (Rogers, Fairbourne and Wolcott, 2011: 39). Rogers et al. (2011, 39) identify micro-franchising as the adequate solution for the above three challenges, adding a fourth aspect:

4) The lack of MNC's understanding or ability to operate successfully in the vastly different context.

Hürlimann (2011: 4) complements these assumptions by referring to micro-franchising as a solution for large enterprises to get access to markets that they would not be able to tap into themselves due to their cost structure. Gibson (2007:24) additionally stresses that buying a well-established franchise cuts down on the business failure rate thanks to the defining characteristic of the franchise model: the franchisor has already been through the process of discovering the majority of the problems with running the business and has taken care of them in his own operation before starting to franchise. Consequently franchisees buy an already-tested business model and reduce thereby the risk of failure (Gibson, 2007: 24).

2.2. Context: the informal market

Traditional franchising literature has been developed assuming a formal, high-scale economy as

[3] Prahalad (2009: 28) illustrate the distribution of wealth and the capacity to generate incomes in the world in the form of an economic pyramid. The 4 billion people living on less than 2$ a day constitute thereby the *bottom of the pyramid* (BOP).

the operational environment. Micro-franchising is set to work in the BOP market, where the informal economy makes up for the largest part. The informal market has been recognized as one of the biggest development challenges currently facing the developing world (Henriques and Herr, 2007: 43). Research indicates that barriers to entrepreneurial activity in those markets include: the lack of access to capital, the lack of education and skills, weak networks, poor working conditions, limited resources and marketing, limited training, low innovation, legal issues, and high levels of harassment by authorities (Henriques and Herr, 2007: 46ff.)

Theories of business operations have generally been formulated in the context of the economically advanced nations. Given the contrasting conditions of the developing world's business environment, current theory does not adequately explain the best way to operate in BOP markets (Jensen and Sutter, 2008: 192). Nevertheless micro-franchising literature assumes to partly provide mechanisms to overcome the above described constraints, as by design micro-franchising enhances businesses and addresses barriers to employment and market entry. These benefits occur when the franchise opportunity enables a micro-franchisee to access established networks, supply chains, and marketing options provided by the franchisor. Micro-franchising also links individuals to the formal economy when the parent organization operates in it. As such, being involved in a micro-franchise, one benefits from legal standing and legitimacy (market securities, legal protection as a certified vendor etc.) and gains access to knowledge and training covering for the lack of education and skills (Henriques and Herr, 2007: 48f; Jonson Christensen et al., 2010: 596).

Of particular importance for our analysis are the implications derived from the theoretical discussion on the issue of infrastructure. BOP markets lack the infrastructure required by firms in traditional markets - from roads, railways, electricity to communication systems. Businesses therefore face distribution and production challenges as they attempt to build their presence in these areas (Jensen and Sutter, 2008: 198). Chikweche and Fletcher (2011: 343) see franchising as a distribution strategy, which firms can use to enhance distribution at the BOP. Gibson (2007: 34) argues in the same direction by declaring that micro-franchising does not only work in large cities but also in very remote locations. On the other hand Jensen and Sutter (2009: 198) state infrastructure and corruption as the two contextual factors, which cannot easily be mitigated by micro-franchising, despite being considerable. These conflicting assumptions should be kept in mind to approach the issue at-hand while analyzing best practice cases.

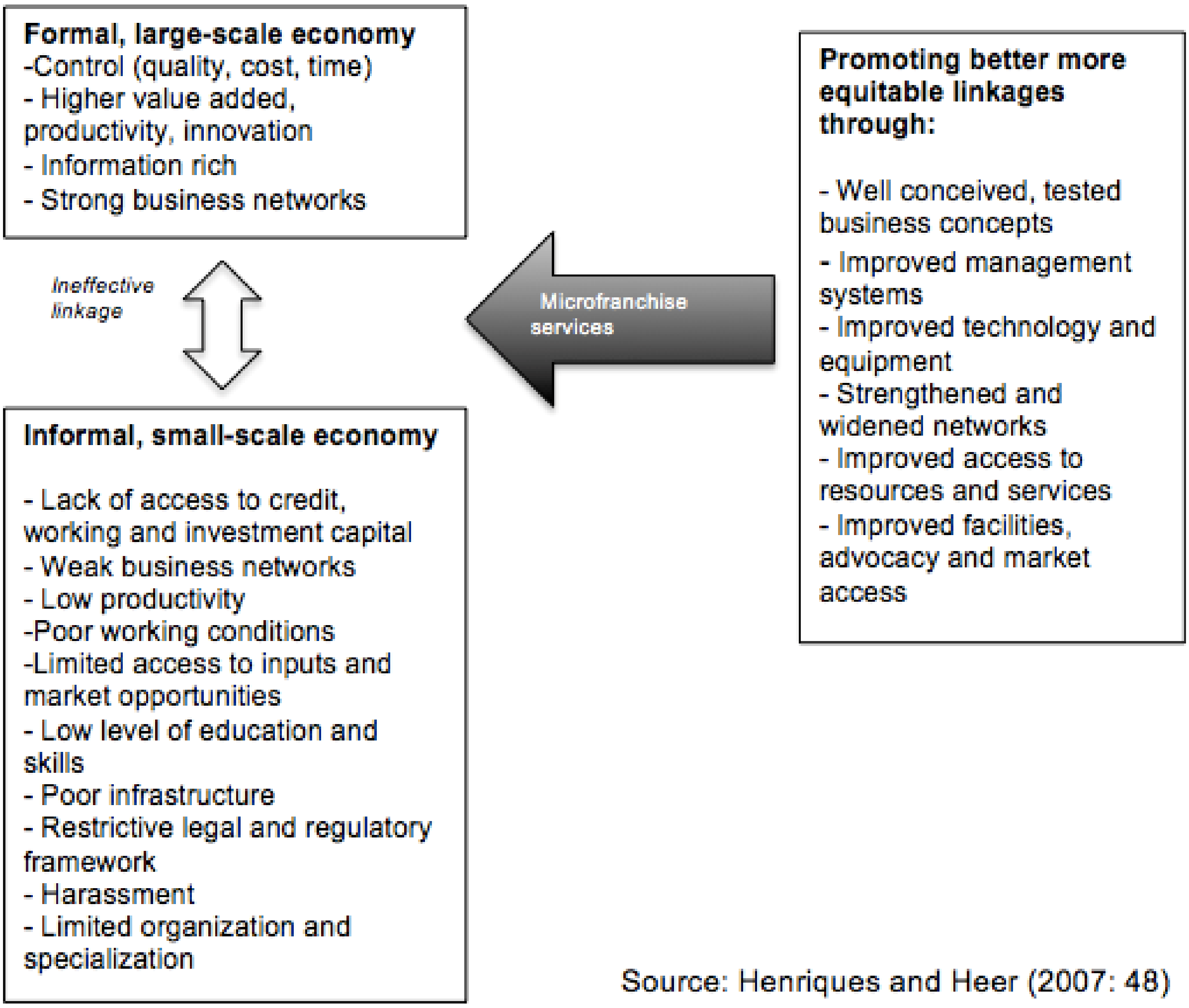

Figure 2: Micro-Franchising as a tool to connect the informal economy

2.3. Micro–Franchising distinctions

Although traditional franchising provides the business model, there are important adaptions to the concept in micro-franchising, accounting for the different contextual situation and the underlying social objective:

Adaptation relating to size

The adaption relating to size is the most obvious one, considering the prefix "micro". The average US franchise costs roughly 250'000 $, whereas micro-franchise startup costs range from 25 – 25'000 $ (Fairbourne, 2007; Jones Christensen et al., 2010).

Adaptation relating to financial structure

Another significant modification of the Western franchise model concerns the issue of profit for the franchisor (Jonson Christensen et al., 2010: 596). The literature distinguishes three main types of the financial support structure, reflecting to a large part the varying degree of benevolent motives behind establishing a franchise:

1) *Social micro-franchising:* The dominant objectives are to provide goods and services at an affordable price and to create jobs at the BOP. The model operates off of a financial model that is not focused on sustainability. A continuous flow of funds into the project is needed, since product costs are subsidized in order to reach the objectives (Fairbourne, 2007: 10).

2) *Sustainable micro-franchising*: Sustainable micro-franchises pursuits the objective to create profit for the micro-franchisee and enough surplus profit to sustain the micro-franchisor, while providing goods and services at an equitable price (Fairbourne, 2007: 10f.)

3) *For-profit micro-franchising:* This model is very similar to sustainable franchising with one added variable - to create enough profit for the micro-franchisor to return profit to investors. This model requires much higher start-up capital in order to scale quickly and become profitable enough to repay investors. Even within the sustainable micro-franchise model, sustainability may not occur until the franchise system has grown to a sustainable point, meaning until it has a certain number of franchisees operating franchises that pay fees (Fairbourne, 2007: 11).

Adaptation relating to the nature of the franchisor

How much emphasis is put on the social objectives and how much on profitability and returns to the franchisor depends strongly on the characteristics of the franchisor. This constitutes another key modification to the traditional franchise model. Generally, micro–franchise relationships are initiated by franchisors who are either independent business people, NGOs or MNCs.

1) *Independent micro-enterprise owners as franchisors:* Independent micro-entrepreneurs can turn to micro–franchising after having accumulated enough business experience, clientele and capital to expand into multiple locations. So each time they sell a new franchise, they gain another location, which helps the business increase its market share. They gain consistent paying customers, royalty fees and franchise fees and the opportunity to build a strong brand and to expand the franchise's product-distribution channel (Gibson, 2007: 27).

2) *NGOs:* In recent years NGOs have discovered micro–franchising as a method to get involved in the development process. From the NGOs perspective micro–franchising is all about helping struggling necessity entrepreneurs by giving them another alterative. NGOs typically assume their franchisor role by creating a business from scratch and replicating it, or investing in a struggling micro-enterprise that has potential for growth and help that business become a micro-franchise network (Gibson, 2007: 27).

3) *MNCs:* In recent years powerful businesses have recognized that profits can be made in markets other than those in the developing world. Realizing that the four billion people who find themselves at the base of the economic pyramid have basic needs that are not met yet, they are expanding their efforts into these new markets (Gibson, 2007: 27).

2.4. Implications for success

So far the theoretical discussion identifies crucial requirements for a micro-franchise to work from the perspective of the literature:

In order for micro-franchising to be successful, the business that is to be replicated must have proven itself to be worthy of it. It must present a good developed, established, sustainable model and rely on prone local needs (Gibson, 2007: 25, Rogers et al., 2011: 37).

Furthermore there are requirements for potential products and services to be distributed through the franchising model. Micro-franchising operates usually in areas where people mostly have no or little education, which restricts the complexity of the product considerably. The product must be very simple to understand. No higher education should be required to explain and sell the product/service. Even if the franchisee understands it, chances are that his costumers will not, in which case they will not buy them (Hürlimann, 2011: 15f.)

Financial success of the franchisor is tied directly to the financial success of the franchisee. Thus the micro-franchisor has a significant interest in seeing the micro-franchisees get the support, training and mentoring they need (Gibson, 2007: 34ff.) The micro-franchisor primarily seeks entrepreneurial managers in franchisees. The operational theory behind micro-franchising is the belief that management is a skill that is eminently trainable. NGOs concerns for the micro-franchisees to be successful are even heightened by their explicit goal to foster entrepreneurship and self-reliance of the franchisees (Jones Christensen et al., 2010: 596).

<table>
<tr><th></th><th>Franchising theory</th><th>Micro-Franchising theory</th></tr>
<tr><td>Goal of business</td><td>Economic considerations:
Growth of business/profit</td><td>Economic considerations:
Growth of business/profit
Social considerations:
Poverty alleviation</td></tr>
<tr><td rowspan="2">Why chose franchising?</td><td>Resource Scarcity theory:
Franchisee brings either financial or human capital in order to achieve rapid scale-up.</td><td>Economic considerations:
Provides access to the BOP market</td></tr>
<tr><td>Agency theory:
Savings in monitoring costs by resolving horizontal-agency problems.</td><td>Social considerations:
Potential to turn necessity entrepreneurs to self-reliant franchisees, creates jobs, makes goods and services available for the poor</td></tr>
<tr><td rowspan="4">Premises to be met</td><td colspan="2">Functioning, sustainable business model:
- profitability
- existing market demand
- established operational procedures
- marketing and sales strategy
- etc.</td></tr>
<tr><td rowspan="2">Franchisee bears entrepreneurial risk</td><td>Simplicity of product, business model</td></tr>
<tr><td>Possibility of subsidies during early stages of micro-franchisee life-cycle</td></tr>
<tr><td>Nature of product matters:
→ interest alignment in order to resolve vertical-agency problems (e.g. repeat customers; ongoing support; quasi-rents)</td><td>Nature of product matters:
→ reduce franchisee risk related to lack of “diversification” through stable revenue streams (e.g. repeat customers)</td></tr>
</table>

Figure 3: Overview theory

3. Best-Practices in Micro-Franchising

Based on the theoretical considerations of the franchising and micro-franchising literature, this section aims to identify best-practices of current ongoing micro-franchising projects as several micro-franchising businesses have emerged within the last 20 years. Beyond the theoretical framework, it is their business design and management, their operating experience, their achievements and business breakdowns which provide the best overview for defining general criteria for success in the micro-franchising business. To do so, this analysis is based on the database of 18 micro-franchising businesses established by Fundes.

As such, we start by presenting our main findings from the analysis of currently existing micro-franchises. We then identify and explain in detail the main criteria for success for micro-franchising which the SDC needs to bear in mind when designing micro-franchise businesses as development aid tool.

3.1 Overview of the main findings on Micro-Franchising

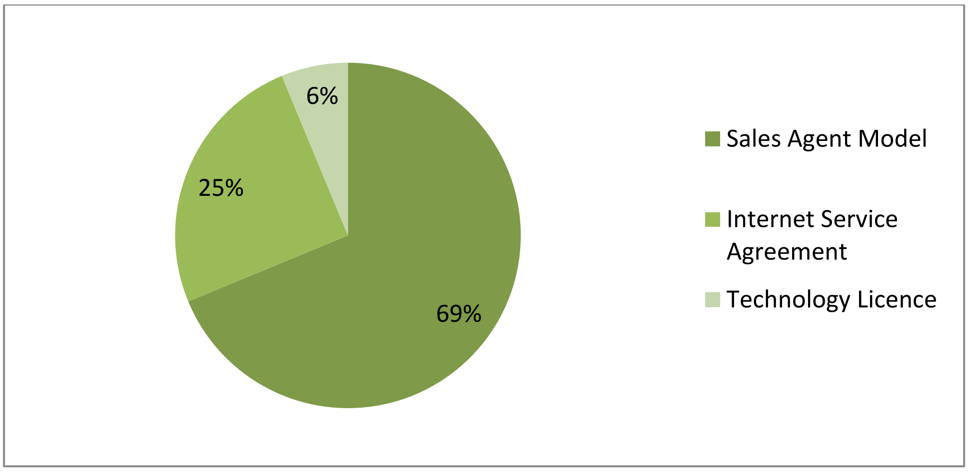

Figure 4: Cases by business model

Finding 1: Over two thirds of the successful micro-franchising projects are based on a classical sales agent model (e.g door-to-door selling, etc.). Internet service based models in India, which are often adaptations of the sales agent model to services, represent 25% of the successful projects considered Technology based approaches due to turn-key, cost and tipping point issues are only representing 6% of the analyzed projects.

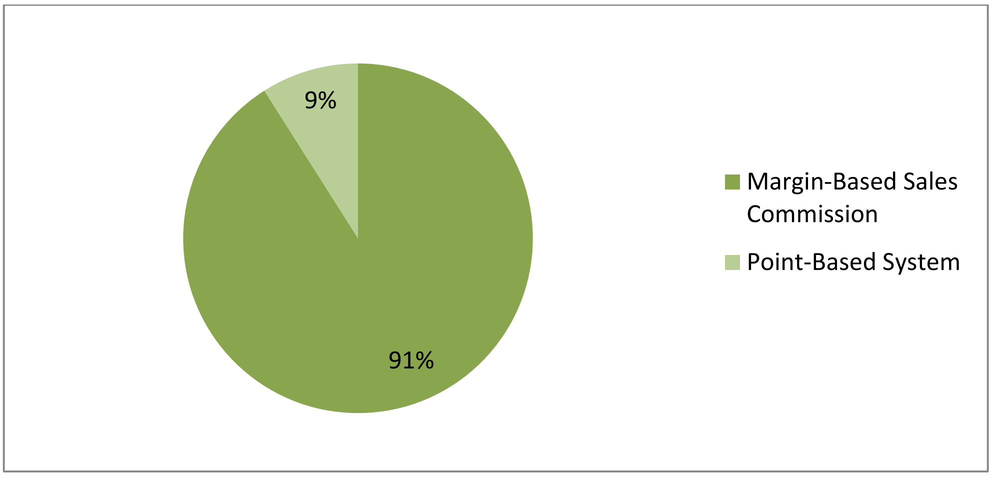

Figure 5: Cases by compensation scheme

Finding 2: The relative importance of sales agent models is also reflected in the predominance of margin-based sales commission payment schemes. Due to the fact that projects need to focus on easy, transparent and feasible business-models, the margin based sales commissions approach appears to prove itself as best fit for micro-franchising projects. While this finding is in opposition to the franchising literature as royalty-based compensation models do not exist in micro-franchising, it confirms micro-franchising theory in its aim for simple interest alignments.

	NGO	**Company**
Imported	**Living Goods** **Health Store Foundation**	**Shakti** **Semilla**
Local	**KickStart** **Lijiat Papad** **Tosepan Pajti** **Drishtee**	**Constructiva** **Patrimonio Hoy** **Fan Milk** **Mi Tienda** **Vodacom** **N-Logue**

Figure 6: Cases by background

Finding 3: Local initiatives of micro franchising, whether for-profit corporations or non-profit NGOs, seem to be prevalent, dominating over their "imported/external" business homologues. This might be due to the fact that one of the most important criteria of success for launching a micro-franchising project is the local knowledge of the BOP target market as well as the local adaption of products and marketing initiatives.

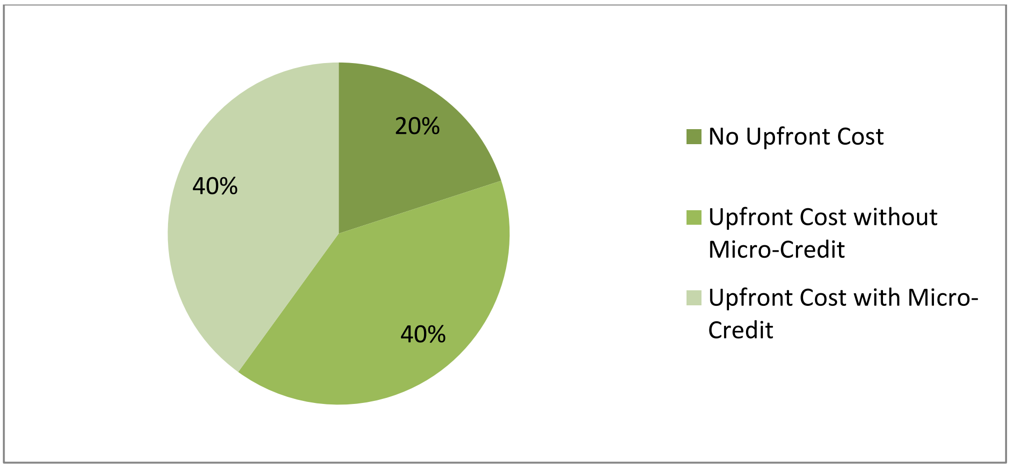

Figure 7: Cases by upfront costs

Finding 4: Because of the strong theoretical conception of micro-franchising as combination of a business in a box and micro-finance, one would have expected to have a majority of micro-finance based projects. The analysis showed a more differentiated picture. Projects without upfront cost are clearly in the minority but nevertheless it seems that projects often do not need micro-credit funding (due to startup capital available for franchisees or external donations).

Positive Achievements	Business Drawbacks
- **Stable Revenue Stream with fast-moving consumer goods** (Shakti, Grameen Phone, Drishtee) - **Local Adaptation of Product** (Shakti, Patrimonio Hoy, Lijjat Papad, Mi Tienda, Semilla, Fan Milk, Grameen Phone) - **Efficient Distribution Network** (Shakti, Fan Milk, Mi Tienda, Living Goods, Health Store Foundation) – Consumer Goods - **Good Branding** (Living Goods, Mi Tienda, Shakti, Semilla, Fan Milk, Constructiva, Drishtee, Lijjat Papad) - **Diversification Strategy** (Drishtee, Mi Tienda)	- **Lack of Profit: Sustainability threatened by dependency on Subsidies** (Shakti, Health Store Foundation, Kick Start, Grameen Phone, Honey Care Africa, n-Logue, Constructiva, Drishtee, Living Goods, Tosepan Pajti, Lijjat Papad) - **Unstable Revenue Stream** (n-Logue, Patrimonio Hoy, Constructiva) - **Inability to adjust to market trends** (Grameen Phone, n-Logue) – Counter-example is Drishtee having developed 30 different business models - **Difficulties in Monitoring** (Fan Milk) - **Lack of sales skills** (Patrimonio Hoy) - **Competition with local Government** (Patrimonio Hoy)

Figure 8: Overview best-practices

Finding 5: If we assess more in detail the respective achievements and business drawbacks of micro-franchising projects, we see that almost all micro-franchising projects face the problem of a lack of profits which undermines the sustainability of those projects due to the dependency on subsidies. Furthermore, unstable revenue streams have been a recurrent problem for micro-franchising of construction materials while internet service providers faced the problem of being unable to adjust to the market. On the other hand, the stable revenue stream to consumer goods, the adaptation of the business to local needs, the product marketing, and efficient distribution networks have been the most important success factors for micro-franchising projects.

3.2 Business Model

Viable For-Profit Business Model

Micro-franchising should be based on a viable business model. In consistence with the franchising and micro-franchising theory, all micro-franchising businesses rely on a social business which proves the actual demand for the product or service at the bottom of the pyramid and therefore its economic or social viability. A common mistake has been to launch unproven business concepts at the BOP which may endanger the existence of the franchisee who is supposed to trust the business model and to invest in it. The n-Logue micro-franchising project in India underlines this existential mistake. While the business idea to provide internet services to rural areas through internet services in kiosks appeared as a logical BOP-Model, it turned out that the low level of demand (50% of Kiosks reported less than 5 users per day) made break-even impossible. Due to upfront costs of USD1200 financed through micro-credits, several kiosk owners faced severe financial problems. Due to the lack of demand, the business model was not profitable and therefore not sustainable either. As in any business, profitability both for the franchisor as well as the franchisee is indeed necessary to guarantee the longevity of the project, subsidized business models being constrained by the availability of subsidies. Franchisors should therefore directly operate the social business before launching a micro-franchising scheme to scale up the economies as well as the social impact. Only Patrimonio Hoy, Semilla, Fan Milk and Mi Tienda were actually able to scale up micro franchising and to achieve consistent growth.

Dominance of Sales Agent Micro-Franchising Models

In accordance with the Bottom of the Pyramid theory of C.K. Pralahad (2004), micro-franchises are predominantly designed as sales agent models (69%) or internet service providers (25%). There are several reasons for the dominance of sales agent micro-franchising models:

Those business models have the advantage to generate a stable revenue stream in order to provide a stable income to the risk-averse micro-franchisee entrepreneurs. Usually sales agent models are based on FMCG (fast-moving consumer goods) products that have to be purchased on a daily/weekly basis (in opposition to technology based models) and hence guarantee a stable revenue streams for the franchisees who, by definition, are risk averse and dependent on regular incomes.

The fast-moving consumer goods also decrease monitoring costs for franchisors. Micro-franchising of consumer goods or services guarantees repeat customers hence the control of quality is made through the customer himself. This is guaranteed both for sales of consumer goods and the provision of internet services. The Return on Investment (RoI) and product assessment is done immediately after the purchase.

Furthermore, the supply of fast-moving consumer goods creates strong bonds between franchisee and franchisor. Franchisees are dependent on the supply chain and logistic of their franchisor hence drop-out rates are reduced. Consequently, compensation in micro-franchising businesses is almost always made dependent upon sales through margin-based sales commissions (91%).

Success stories for commission-based sales agent models or internet service provisions with stable revenue streams and consequent quality guarantees have been the Shakti (India), Grameen Phone (India), Drishtee (India), Mi Tienda (Mexico), and Sevilla (Mexico) projects.

Challenges to apply micro-franchising for technological products

The aforementioned significance of fast-moving consumer goods as product basis for micro-franchising businesses also implies the general inapplicability of micro-franchising to the distribution of technologies. The promotion of technologies through micro-franchising faces three main issues:

The first issue is linked to the necessity of stable revenue streams as aforesaid in the last section. Due to the nature of technologies, demand is extremely cyclical. Live-changing technologies are usually perceived as long-term investments with a life-cycle of over 15 years. Therefore, technology-based sales models face extremely unstable revenue streams for the franchisee and can thus only be a side-business for him.

Furthermore, monitoring and quality insurance is a major concern for technology-based models. Due to the long life-cycle of the products, monitoring cannot originate from repeat customers who would signal through their continuous purchases their satisfaction to the franchisee as well as the franchisor. On the other hand, high upfront costs require a strict guarantee of quality. Defective products will not only harm the families that purchased the good but also impact the credibility and branding of the franchisor.

Last but not least, the generally high upfront costs for technological products are constraining the demand at the bottom of the pyramid. Consumers at the BOP are neither able to afford such cost-intensive technologies due to a lack of savings nor to plan in such long-term horizons. Furthermore, their willingness to pay for such life-saving technologies may be constrained. While low income consumers often recognize the need for and the benefits of those technologies, they may rank lower in terms of their priorities compared to traditional consumer goods.[4] This discrepancy between their desires and needs can for instance be observed in the impressive expansion of the mobile phone market in developing countries while water purifiers, household solar electricity systems or other life-changing technologies remain marginalized sales products.

Technology-based micro-franchising models therefore need to invest into social marketing campaigns raising the awareness but also to develop innovative product solutions adapting their technologies to the BOP consumers and their ability to pay, for instance by providing product and service "packages" such as product leasing or temporary free trials of products combined with quality guarantees and maintenance services. In turn, the compensation system needs to be innovated as well. One innovative approach is followed by Patrimonio Hoy with its point-based commission system which not only pays franchisees for the customer acquisition but also for customer retention and satisfaction. We will further elaborate those ideas of "social marketing", "product adaptation" and "technology packaging" in the next chapters.

3.3 Marketing

Social Marketing to Raise Awareness

The BOP markets have their own specificities: demand for products does not always exist (e.g. lack of awareness) or is insufficient (e.g. tipping point concept based business models). FMCG consumer goods and construction materials as offered by Shakti, Semilla, Mi Tienda or Constructiva can be promoted through ordinary marketing and branding whereas on the other hand social businesses, which aim to promote life-changing products, need to invest in social marketing as it requires awareness raising among the rural poor and sometimes even offering samples so that they may try the product by themselves (Heierli 2008).

[4] http://businessinnovationfacility.org/profiles/blogs/willingness-to-pay-for-clean-water

It is important to remember that the promotion channels in BOP countries differ from those used in advanced economies: billboard and broadcasting campaigns have a limited impact. In the BOP countries product promotion is usually undertaken through existing retail shops or through selected stakeholders (e.g. doctors, teachers, religious leaders or village leaders). The word-of-mouth propaganda is thereby one of the most efficient tools, which reinforces the necessity of simple and useful products. This promotion requires thorough market research to understand consumer's needs. Social marketing is about raising awareness and changing traditional habits through rational educational campaigns and irrational instruments as mounting social pressure.

As some products and services require a change of paradigm for the local population, one has to bear in mind that selling those life changing products/services, even at a low price, to the customer will require important marketing efforts and investments from the franchisor.

Customized Products

In line with the specificities of the BOP Markets highlighted by C.K. Pralahad (2004), micro-franchising business have to adapt their products to the specific consumer needs and habits if they want to target the BOP consumer segment.
Customers of the BOP markets, due to their low and unstable revenue streams prefer single-unit sales (Shakti) with smaller sized packaging (Semilla, Mi Tienda). Bulk buying for consumers, even though it would reduce the cost per unit of the purchased goods does not apply in the BOP markets.

Given this unique market demand, there is a need for micro-franchising initiatives to develop customized products and business models adapted to the local demand.

Brand development

Branding is a key part of efficient micro-franchising initiatives. Similar to traditional franchises, micro-franchising businesses are generally been built on strong brands and require extensive and continuous marketing campaigns.
As already stated earlier on, franchisees are risk averse and have to balance out the pros and cons before joining a micro-franchising business. Hence any micro-franchising initiator requires a strong brand and stellar reputation in order to balance out the initial lack of trust that entrepreneurs and potential franchisees might have. Once a strong brand is established, the

franchisors ought to make sure, through quality control and continuous marketing campaigns that this strong brand remains.

3.4 Supply Chains

Efficient Supply Chain

Due to small margins in micro-franchising models, innovative and efficient supply chains are one of the most critical factors of success. Indeed, all successful micro-franchising businesses rely on an efficient distribution network with a flat hierarchy. There are different supply chains organizations according to the product they distribute which we will illustrate on the basis of Mi Tienda and KickStart.

Mi Tienda is a privately held rural distribution company in Mexico focusing on the over 600.000 small scale retailers in the rural market. Their micro-franchising business strategy is to effectively exploit the BOP market opportunities. Rural family-run grocery stores are essential for supplying goods to the low income rural communities. However, high transportation costs because of the long supply chain and the lack of economies of scale due to low weekly store purchases constrained their business growth. Mi Tienda offers a distinctive micro-franchising solution which circumvents intermediaries in the supply chain and offers door-to-door delivery of individual items within 48 hours thereby avoiding bulk purchases for the retailers which would incur high working capital expenses. Mi Tienda has therefore built an efficient distribution network based on central warehouses which stock bulk purchases of non-perishable goods. Those goods are delivered in single units once or twice a week to over 700 rural stores, simultaneously taking new orders. Economies of scale and consequent operating efficiencies of the supply chain are based on the density of rural villages in Mexico reducing transportation costs. This distribution network in the densely rural village area of Mexico is illustrated below in the expansion map of Mi Tienda.

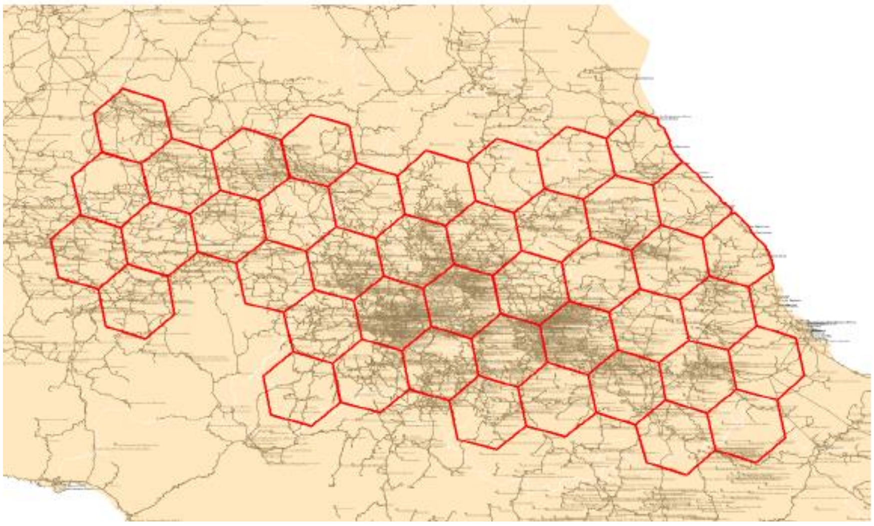

Figure 9: Distribution Network Zones MiTienda

The second example and at the same time "anti-example" would be the supply chain of KickStart, a Kenyan NGO that promotes economic growth and employment generation. KickStart aims to development and license technologies that local entrepreneurs can use to establish profitable small-scale businesses. This supply chain management has the uniqueness of focusing on the first and last stages of the supply chain: they focus only on the R&D and market research, completely outsourcing the product and distribution to the private sector supply chains that exist. In order to ensure demand for the products, assess and monitor the quality of the products and to understand the needs customers, KickStart also manages the last part of the supply chain. This unique model allows specializations for the franchisor while generating employment creation and private sector supply chains.

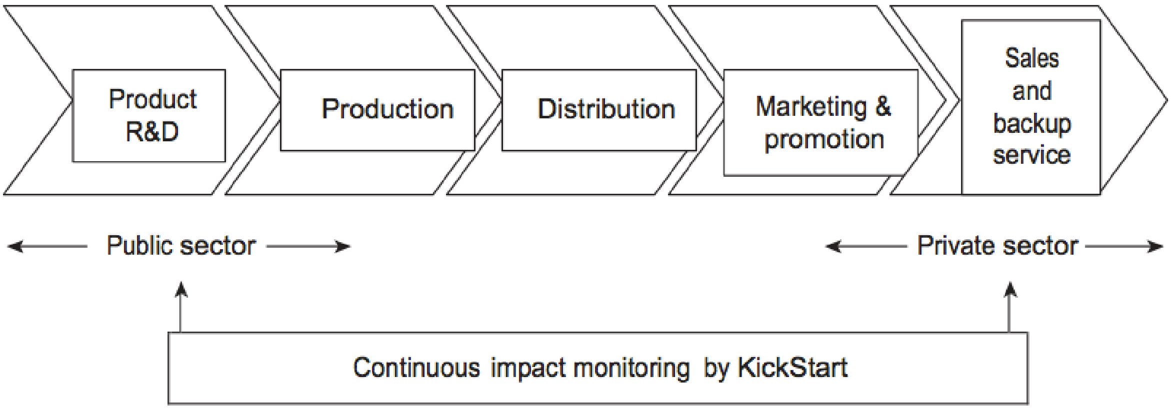

Figure 10: Supply-chain KickStart

Standardized procedures

Franchisors need to provide a "business in a box" to the BOP franchisees. Contrary to the classical franchising business, the Franchisor has to develop the entire product design and local sales models as franchisees have generally no entrepreneurial experience (lack of accounting skills, business experiences, etc). Therefore the mutual cooperation and trust-building measures between franchisor and franchisee turns out to be crucial for the successful micro-franchising. Standardized products and equipment are not only necessary due to the lack of entrepreneurial expertise but also in order to ensure that quality standards are respected and that a the homogeneous supply chain is running smoothly.

Providing a formula including standardized products and equipment as well as clear and simple instructions materials are key.

3.5 Franchisee-Profile

Training and communication

As it is probably the first time that the franchisees run a business, training them is a key part of the micro-franchising project. Therefore training and pro-active communication with franchisees plays a crucial role.

The education levels and knowledge background is going to vary from one franchisees to another but some basics have to be respected: franchisees must be motivated, understand the benefit and rules of the micro-franchising agreements and be given training adequate to the followed business models. Franchisees should be able to understand the basics of their new business and be able to anticipate market and customer changes.

Regular communication with franchisees is required due to the fact that the inability to adjust to market trends is one of the most recurrent origins of failures for micro-franchising businesses, as in the case of Grameen Phone and N-Logue. On the other hand, micro-franchising business with diversification strategies as Drishtee and Mi Tienda were able to sustain their business.

This experience shows that the franchisor has to invest into the central business innovation and diversification of micro-franchising in order to sustain and expand the micro-franchising model. Micro-franchisees due to their social position often lack the ability to generate innovation (e.g

KickStart) on their own nevertheless the development of innovative ideas should be developed in close cooperation with the micro-franchisees who have the knowledge on the local market.

3.6 Criteria of success for micro-franchising projects

Hence to summarize our criteria of success, we developed a brief checklist that every successful micro-franchising project should have:

Business Model:

- ✓ Sustainable and for-profit business model based on existing demand for product
- ✓ Sales-Agent Models for fast-moving consumer goods which procure stable revenue streams thereby creating income security and interest alignment
- ✓ Incentive-Based Payment Schemes for Franchisees

Product:

- ✓ Social Marketing of Product raising Awareness
- ✓ Locally Adapted Products
- ✓ Strong Branding

Distribution Networks:

- ✓ Horizontally Flat Distribution Network
- ✓ Standardized Products

Costs:

- ✓ Low upfront costs
- ✓ Provision of Micro-Finance Solutions
- ✓ Training and Trust-Building

Macroeconomic Conditions:

- ✓ Existing Demand
- ✓ Infrastructure
- ✓ Dense Population / Urbanization

4. Potential micro-franchised SDC projects

After having reviewed the current literature and having highlighted the criteria's of success of previous successful micro-franchising projects, we now aim to find projects supported by the SDC that could prove suitable for micro-franchise use.
For that we will analyze one FMCG (fast-moving consumer good) and one technology based project.

4.1 Aqua+ : Water purification for the BOP markets

The "Aqua+" product owned by Tara in India and based on the WATA technology developed by Antenna Technologies in Geneva could prove to be a potential successful candidate for a micro-franchising distribution model. We will try to briefly analyze why and how Aqua+ could be adapted to a micro-franchising business model. Our analysis is based on the reports and interviews provided by Antenna Technologies in Geneva. In this context, we would like to thank Ms. Fanny Boulloud for her time and efforts.

The problems with water purification in BOP countries

The availability of water remains a crucial issue for BOP countries and there have already been several non-coordinated development initiatives aiming at resolving the issue, such as ultraviolet purifiers and filters (Tata Swach), chlorine capsules and other products. All of those faced either cost problems (being too expensive for the poor of BOP) or limited effectiveness. Tara's Aqua+ product aims to resolve this dilemma.

Tara, a social enterprise of the DA group has a special focus on Water, Sanitation and Hygiene (WASH) at the BOP. In order to develop an effective, cheap and simple water purification system for the poorest of the poor in the BOP markets, Tara teamed up with Antenna Technologies, a Geneva based foundation that provided the required WATA technology. The results of this cooperation are the Aqua+ bottles of Sodium Hypochlorite Solution (liquid chlorine) that are to be used as point of use water disinfection products.
A 50ml Aqua+ bottle is currently priced at INR 30 and can provide 500 liters of pure water, enough water for one month for a family of 5 members. Given to those capacities, Aqua+ can be considered to be the cheapest solution on the market of water purification reducing the cost of pure water to INR 0,06/Liter.

Why Aqua+ could be applied for micro franchising

Aqua+ is a classical FMCG (fast-moving consumer goods) with monthly repeated purchases that could be sold through a sales agent model (as a reminder 69% of the successful micro-franchising projects are based on sales agent models). Aqua+ can guarantee through its repeated purchases a stable revenue stream for the franchisee, which is a key factor for the franchisee. Furthermore, due to the repeated purchases but also the simplicity and user-friendly usage, Aqua+ allows for immediate quality control by the customers. Any incidents of inefficiency in water purification would have dramatic reputational consequences for the product but also for the franchisee as his client base would be undermined. Hence monitoring cost for the franchisor are limited.

Having a shelf life of six months, a 0,06RS/Liter cost, Aqua+ proves to be appealing for the BOP market as it is an affordable water purification method which targets the needs of the working poor with a monthly household income of less than RS 6000.

As best practices have shown, sustainable business models and product lines are primordial for future evolution. Tara has in the past increased the price, reacting to local demand and willingness to pay, in order to ensure that the product is available for those with low incomes while at the same time ensuring that a sufficient margin exists. Therefore all stakeholders in the supply chain can be rewarded accordingly, ensuring long-term sustainability and prosperity.

Awareness problems and social marketing

Creating awareness is the fundament of the promotion of socially useful micro-franchising initiatives. Often people do not know of the dangers of unpurified water following the "it has always been like that" approach. Hence there is a need for promotional campaigns (stickers, posters, interactive workshops within communities) that aim increasing awareness. The IPSOS has undertaken a market research for Tara highlighting the instruments of social marketing. Emotional arguments, such as the health of their children, combined with economic rationality (reduced medical bills and more working days) seem to raise awareness as well as the social need for water purifiers.

Beyond social marketing, there is a need for constant brand marketing if TARA aims for a successful and sustainable product. This needs to be undertaken by promoting Aqua+ as the water purification product for the daily use, simple, cheap and safe. Furthermore Tara currently works on innovative marketing ideas such as using different sizes of bottles, improvement of product features as packaging, bottle design, etc. Currently a creative collaboration aiming at developing bottles that can be re-used as toys is undertaken in collaboration with the Design Management Centre at University of applied Science in Luzern.

Aqua+ current business model ideas

The recent thoughts of Tara and Antenna Technologies to propose an integrated business model to distribution partners are already very close to a micro-franchise sales agent business model. We believe that some ideas from the concept of micro-franchising may be taken into consideration in order to scale up the distribution of Aqua+ more effectively.

TARA aims to promote Aqua+ through licensing and product procurement to various grass-root organizations like NGOs, commercial distributors and local social businesses in order to tap into their existing delivery channels. Similarly to other projects like KickStart, Aqua+ should be distributed through private supply chains which would avoid extensive efforts building up a new one. Those distribution channel partners will figure as franchisors to which TARA proposes an integrated micro-franchising business solution.

The channel partner should engage regional managers who are responsible for setting up, managing, and monitoring a local micro-franchising distribution model of approximate 5 sales agents. For this work he would receive a fixed salary (Rs 5000/month) and sales-based incentives of Rs 0,5 per bottle sold. On the local level, sales agents would figure as franchisees accessing up to 4000 households within their community. They will be granted a limited allowance of RS 1000 per month in order to cover the expenses and will be rewarded through direct commission per bottle sold (Rs 4 per bottle). In the business model from TARA, those sales agents are furthermore responsible for the development and management of a network of retail stores selling Aqua+. For each bottle sold through retail stores, they will receive an indirect commission of Rs 2 per bottle. This should incentivize the franchisee to develop the system of retail stores and to convince BOP customers to buy Aqua+ from retail stores on a regular basis. On the last level, the retail agent sells Aqua+ products and therefore receives a sales commission of RS4 for every bottle sold. This represents a quasi-micro-franchising business within the micro-franchising distribution model, as the sales agent is the quasi-franchisor for retail stores guaranteeing the product procurement as well as marketing solutions.

Figure 11: Distribution Aqua+

Source: Boulloud, Fanny (2014) – Undisclosed Working Paper

We believe that the current business model project is going into the right direction of a micro-franchising business, the channel partner being the franchisor and the sales agents as well as retail shops being franchisees. However, from the best-practices of micro-franchising, we would like to suggest some considerations for the conception of this integrated micro-franchising business model for local distribution channels.

First, in order that this strategy of TARA (Licensing and Procurement of Aqua+ to existing Distribution Channels) may work, TARA has to build a strong brand with Aqua+ which is so far not taken for granted. This is necessary in order to gain partners with distribution channels who want to invest into this social business. But it is also required within the micro-franchising in order to attract sales agents as franchisees for distributing Aqua+. Franchisees have to perceive the potential demand for the product. Those sales agents also need to be trained in raising awareness for the issue of water hygiene and for promoting Aqua+. This requires also an investment in the mutual relationship between the manager and the sales agent in order to build trust.

One problem we perceive from the micro-franchising business perspective is the long hierarchies in this system, which is a micro-franchising business within another. The question is whether the sales agent as franchisee of the social business is also the right person to develop the network of retail stores. First, the issue is whether a sales agent may have the knowledge and force of persuasion to build a partnership with retail sellers, to help them with the promotion within the retail store, and to monitor their activities. Besides this probable incapacity to develop such trustful franchisor-franchisee relations, the question is also how the distribution channel will be able to monitor the sales agent. The sales agent may for instance claim to sell a bigger share of Aqua+ through retail stores than is actually the case. Then he would get Rs. 6 per bottle out of which he would have to distribute Rs 4 to the retail seller, who may not exist. The sales agent may also make his own deals with the retailer, or may operate his own retail store.

Finally, the concept to increase progressively the sales volumes by passing consumers from direct purchases from the sales agent to repeat purchases in retail stores in the intermediate and mature stage is a logic process of scaling up distribution. However, this model ignores the fact that sales agents have less incentive to pass from the intermediate stage to the mature stage of distribution as the proposed commission system per bottle sold is less attractive for sales agents if a majority of customers buy from retail stores (Rs. 2 / bottle) and no more customers can be won as the market is already oversaturated. The difference in commission may lead to the problem that sales agents may prefer rather direct selling than indirect selling through retail stores.

We therefore believe that the hierarchy is too complicated. Instead of sales agents being responsible for the retail stores, one may think about a parallel micro-franchising system in which the manager from the social business administers directly both sales agents and retailers as separate franchisees. One may also think about a different compensation scheme for sales agents. As the idea is to win as many customers as possible for constantly using Aqua+, one may think about the point-based compensation system of Patrimonio Hoy in Mexico, where the acquisition as well as the retention of customers is rewarded. This is also the case in the current conception with the indirect commission of Rs 2 per bottle sold in retail stores. However, as explained, there are serious risks of fraud due to a lack of control on the supply chain.

4.2 Oolux: Solar panel leasing

The problem of capital goods

Our combined findings from theory and case study analysis indicate that using micro-franchising as a distribution model for capital goods can be problematic. This can be attributed to two main issues.

Firstly, the distribution of capital-goods, either through sales or through decentralized-production, implies relatively high upfront costs for a given micro-franchise, be this in the form of investment in stock or in production facilities. As such, the entrepreneurial risk for a given micro-franchisee is especially high, seeing as he typically needs to invest a substantial proportion of his life savings into the franchise. This is often exacerbated, due to the fact that many capital-goods by their very nature do not necessarily achieve a high turn-over rate, which translates into a lack of stable revenue streams (see chapter 1).

Secondly, the low number of repeat customers for a given micro-franchise can result in vertical-agency problems (see chapter 1). This becomes especially problematic if the end-product is supposed to be used over an extended period of time. An example would be that due to timing mismatches between the micro-franchisor and micro-franchisees, the latter free-load on the former's brand building-efforts by producing a product of sub-standard quality (see example Postcosecha). This in turn would imply high-monitoring costs, which would annul one of the main motivations for opting for a micro-franchise business model in the first place.

Despite of these problems, smart-business models can transform capital goods into consumption-goods or services, which address the aforementioned issues, by guaranteeing stable revenue streams (lowering entrepreneurial risk) and resolving timing-mismatches (reducing the potential for vertical-agency problems). As an example of this we consider the case of OOLUX, a project that might be well suited to be developed into a micro-franchising business model.

The case of OOLUX: solar panel leasing

The lack of access to modern, clean energy is a huge challenge for developing countries. The OECD stated in 2010 "the UN Millennium Development Goal of eradicating extreme poverty by 2015 will not be achieved unless substantial progress is made on improving energy access" (OECD/IEA 2010: 237).

OOLUX's objective is "to propose an innovative lighting solution that is adapted to the needs of people without access to electricity living in developing countries" (OOLUX, 2014a). OOLUX is the result of a joint project between Antenna Technologies, Caritas Switzerland and the Bern University of Applied Sciences (OOLUX, 2014a). Together they developed a solar kit, which qualifies through its high quality technology and its modular setup. As we have shown above (see Chapter 2.4) the simplicity of a product is crucial for the success of a micro-franchising business. Through its modularity, OOLUX takes this into consideration and permits furthermore adaptions to different contextual conditions (OOLUX, 2014b and 2014c).
The kit consists of three principal modules: At the heart of the lighting system is a power-box, an intelligent battery with two USB ports. Additionally there is a led lamp, providing a very powerful

lighting source while consuming very little energy. A solar panel as third component completes the system. The costumer has the option to purchase supplementary modules, as for example universal mobile phone adapters or an additional USB hub, which allows multiplying the possibilities of usage (OOLUX, 2014b).

By nature the targeted customer group has no savings and very limited incomes. So OOLUX has come up with an integrated micro-finance solution, distinguishing it from other similar products on the market. This micro-financing system is intended to meet both, customers and suppliers interests (Meli, 2012: 46f).

The micro-finance system allows the customer to acquire an OOLUX kit while paying it off progressively over several months. Hence, the model takes into account the income pattern and spending habits of people by allowing them to pay in instalments of different sizes. So what has been spent on kerosene before, bringing along indoor air pollution, fire and poisoning hazard, can now be spent on clean lightening (Meli, 2012: 31).

The project has so far been launched with retailers as a supplier and is based on a pre-paid model similarly used in mobile phone systems. The retailer activates the solar kit for the duration corresponding to the amount of the payment made by the costumer. When the pre-paid period expires, the system automatically deactivates and the client has to make the payment for the next period in order to continue to use the kit. When the full value of the kit has been paid, the system is activated permanently and can be used indefinitely (OOLUX (2014d). Thereby the system motivates the clients to follow the established payment plan and makes it easier for the retailer to keep track of the payments and minimizes the risk of non-payment (Meli, 2012: 47).

Why would this project be particularly suitable for distribution through micro-franchising?

OOLUX could potentially work as a micro-franchise system, where OOUX as the micro-franchisor, would provide: the product, technical training pertaining to the installation and the maintenance of the product, as well as the financial backing for micro-finance. The micro-franchisee on the other hand would sell, install and maintain the modules and furthermore manage the payments. How would this set-up address the typical issues previously identified in relation to the distribution / production of capital-goods?

Firstly, leasing rather than selling the solar panels implies more stable revenue streams for a potential micro-franchisee, which in turn reduces the entrepreneurial risk he needs to take upon-himself. Secondly, due to the fact that revenues correspond to savings in kerosene, the micro-franchiser has a direct stake in high-quality installation and maintenance of the product. This addresses vertical-agency problems in the form of timing-mismatches. Finally, further vertical-agency problems are addressed by providing quasi-rents making termination threats credible. These quasi-rents are achieved by keeping the monopoly over the product and by providing the micro-financing the end-consumers need in the first place in order to be able to buy the product.

5. Conclusion

The present report has been conducted to provide the SDC with an in-depth analysis of the micro-franchising business model so as to evaluate its applicability as a development tool to provide people at the bottom of the pyramid with socially and economically needed products and services.

By consulting traditional franchising literature we have identified two main arguments for businesses to franchise. In the context of principal-agent considerations, franchising is seen as a solution to align the interests of the franchisor and the franchisee, thereby reducing monitoring costs. Additionally, franchising can also help to overcome resource scarcity by incorporating financial and human capital as well as local knowledge. These benefits cannot be adopted easily into the context of micro-franchising; the micro-franchisee lacks by nature the financial capital to overcome resource scarcity considerations and the usually low educational level makes training and also monitoring often necessary. In order to succeed from a theoretical perspective, a micro-franchise needs to meet the following requirements: Firstly, the business model must have proven itself worthy of replication. Secondly, the nature of the product/service matters considerably, it must be simple and needs to reduce franchisee risks by providing stable revenue streams.

Bearing in mind the recommendations developed in the (micro-) franchising theory, we then decided to base our best practice analysis on the Fundes Database that includes 18 different micro-franchising projects. Through an in detail evaluation of both the theoretical and in-the-field experiences we then developed a check list of our main findings. They revealed that micro-franchising projects usually follow a sales agent model, base their business model on FMCG (fast moving consumer goods) and straight-forward remuneration schemes (margin based commission). Due to the nature of their field of operation (BOP Market, low local knowledge on the products and their uses, etc) franchisors need to acknowledge that extensive efforts in branding, franchisee training combined with social marketing will be needed if the micro-franchising project should kick off.

Last but not least, in order to provide the SDC with some food for thoughts, we looked two ongoing initiatives that we think are potentially suited to be scaled up using micro-franchising. Aqua+, a water purification initiative by Tara and Antenna Technologies, aims at improving the living conditions of the poorest through cheap water purification technologies. After reviewing their current business model projects and having interviewed members of Antenna Technologies we are confident that this product (FMCG) could be distributed through a sales agent business model. Furthermore, as has been shown by our section on solar panel leasing (OOLUX), we showed that despite of some adverse characteristics displayed by capital goods, implementing smart business models can make them suitable for distribution using micro-franchising.

We have provided two project examples of the SDC which we believe would be well suited for micro-franchising solutions in order to scale up their development impact. We are convinced that there are many more options, as for instance the REPIC project in Kenya. However, we urge the SDC to always consider the business logic of micro-franchising as detailed in this report, as there have been several project failures with good ambitions but poor entrepreneurial realization.

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Annex II: Selected case-study analysis based on Fundes

Project	Shakti (India)	Pros	Cons
Business Model	- Sales Agent Model	- Local Adaptation of Product: Standardized and Small Units - Sales margins guarantee profitability for franchisee	- Discount for Stock of Products - Franchisee rotation 50% due to lack of sales skills
Product	- Unilever Consumer Goods		
Stakeholder	- Franchisor: Hindustan Unilever - Franchisee: underprivileged women in rural area		
Compensation	- Margins-Based (7% for Franchisee, 3% Debt Repayment)		
Supply Chain	- Rural Distributor provides stock		
Financing	- Micro-Credit for start-up costs (USD220)		

Project	Patrimonio Hoy (Mexico)	Pros	Cons
Business Model	- Distribution Agreement	- Local Adaptation of construction to aversion for savings through self-help groups	- High drop-out rate of clients (70%) impacting client revenues - Competition with local governments
Product	- Construction Materials and Advice		
Stakeholder	- Franchisor: Cemex - Franchisee: Local Promoters recruiting clients (Self-Help Groups of 3 female Home Owners)		
Compensation	- Point-Based for acquisition, retention and completion		
Supply Chain	- Local network of suppliers and advisors		
Financing	- No start-up costs		

Project	Grameen Phone (Banladesh)	Pros	Cons
Business Model	- Operation of Village Phones	- Adequate Financing tool with weekly repayments - Communication service provides steady revenue stream	- Business model unable to adjust to market evolution
Product	- Public Phone Service		
Stakeholder	- Franchisor: Grameen Phone - Franchisee: Village Phone Operator (Client of Grameen Bank)		
Compensation	- Revenues from phone service as bulk air time purchased with 50% discount		
Supply Chain	- Infrastructure set up		
Financing	- Micro-Credit through Grameen Bank (USD250)		

Project	Semilla (Mexico)	Pros	Cons
Business Model	- Sales Agent Model	- Profit and Social Impact Goals - Motivation through awards to best sales person	-
Product	- Danone Products		
Stakeholder	- Franchisor: Danone - Aggregator: Ashoka FEC		

	- Franchisee: underpriviledged women	- Tri-lateral relationship with aggregation of micro-franchising businesses	
Compensation	- Employment contract with base salary and 15% sales commission		
Supply Chain	-		
Financing	- No start-up costs		

Project	Fan Mild (Ghana)	Pros	Cons
Business Model	- Sales Agent Model	- Efficient Distribution Network with low costs (18%)	- Difficulties in monitoring of quality and respect of expiry dates
Product	- Consumer Goods		
Stakeholder	- Franchisor: Fan Milk - Franchisee: Sales Men		
Compensation	- Upfront payment for products, Revenue Margin (16%)		
Supply Chain	- Efficient Network of Depots		
Financing	- Low Upfront Costs for bike		

Project	Honey Care Africa (Kenya)	Pros	Cons
Business Model	- Production Cooperative	- Simplicity of Production and Equipment	- Change of Model from Micro-Franchising to Cooperative
Product	- Production of Honey		
Stakeholder	- Franchisor: HCA providing bee-hives, equipment and training and purchases production - Franchisee: Small-Scale Farmers		
Compensation	- Selling of Honey to HCA		
Supply Chain	- Mobile Collection of Honey		
Financing	- Start-up costs USD160, Farmers paying only 25%		

Project	n-Logue (India)	Pros	Cons
Business Model	-	-	- Insufficient subsidies for start-up costs - Low number of business (50% less than 5 clients per day) makes break-even impossible - Business model unable to adjust to market evolution
Product	- Internet Connections		
Stakeholder	- Franchisor: n-Logue (Rural Internet Service Provider - Franchisee: Local Service Provider as existing business owners setting up infrastructure providing internet for Kiosks - Franchisee: Kiosk Owners (Men)		
Compensation	- Kiosk Owner: Revenue Stream through Internet Service - LSP: 50% Revenue Share		
Supply Chain	-		
Financing	- LSP: 27% of USD100.000 Investment - Kiosk Owner: USD1.200		

	Investemnt - Micro-Credit with Monthly Payments		

Project	Constructiva (Mexico)	Pros	Cons
Business Model	- Sale and delivery of construction material	- Extra sales volume for Constructiva and the Master Franchisee. - Additional source of income for the POF. - Low cost expansion for Constructiva.	- Less focus on women as micro-franchisees. - Less focus on social benefits by the micro franchise for the microfranchisee. - Focus on clear revenue and cost reduction only.
Product	- Construction Material		
Stakeholder	- Constructiva (Franchisor), ‚Master Franchisee"s and Point of Sales Franchisees that operate an existing business and join Constructiva		
Supply Chain	- Master franchisee handel the delivery and inventory, the POF Franchisee focus on the invoice and transaction.		
Financing	- 4K$ Investment for the POF Franchisee and 30K$ for the Master Franchisee		
Compensation	- 10% Sales Margin		

Project	Health Store Foundation (Kenya)	Pros	Cons
Business Model	- Sale of essential medication model	- HS provides afforable medical care for diseases that generate 70-90% of illnesses and deaths. - A pillar of the health system in Kenya. - Centralized system that ensure good distribution and quality control.	- Economic viability of the enterprise as it operates on donations and makes an annual 1M$ deficit.
Product	- Essential medication for curable disseases		
Stakeholder	- HS as Franchisor with a clinic model franchisee (collaboration with a nurse) or drugstore model (collaboration with a community worker) franchisee. Franchisor focus on collecting donations and growing network.		
Supply Chain	- HS provides with cheap medication and central distribution.		
Financing	- Clinics require 2K$ investment paid by donation, Drugstore require 1,5K$ finance by soft credits (88%).		
Compensation	- Through sales		

Project	Drishtee (India)	Pros	Cons
Business Model	- Sale and Service Model	- Franchisor focused to make franchisees 100% profitable. - Aggressive diversification strategy. - Strong level of	- E-Government proved insufficient hence had to add products and services.
Product	- Create a network of micro entrepreneurs in rural india that sell new products and services in order to empower communities.		
Stakeholder	- Drishtee (Franchisor) in collaboration with relevant NGO's		

	and ministries. Kiosk and VRC franchisees who are local residents.	support for franchisees.	
Supply Chain	- Drishtee offers over 30 different business models for the franchisees		
Financing	-		
Compensation	- 80% sales margin for franchisees and 20% for franchisor.		

Project	**Kickstart (Africa)**	**Pros**	**Cons**
Business Model	- Promotion of economic growth and employment generation	- Creates micro-enterprises. - Kickstart focuses on core competencies (detecting market needs and crafting technology)	- Kickstart does not operate as a franchise. - Need for constant donation to cover the losses. - High cost of some products, companies did not create new product lines and were not able to grow.
Product	- Technological tools designed for the market		
Stakeholder	- Kickstart which designs the technology in the US, grants licenses and collects donations. Licensing Manufacturers produce the good, licensing distributors sell the products.		
Supply Chain	- Kickstart uses the supply chain of private sector businesses		
Financing	-		
Compensation	- 5$ margin for produced goods and 28$ margin for sold goods. Only 10% margin for Franchisor.		

Project	**Living Goods (Uganda)**	**Pros**	**Cons**
Business Model	- Avon Direct Sales Model	- Improve weak local medical distribution system. - Good branding, operation system and quality guidelines.	- Need of donations to cover up the costs.
Product	- Health Related Products and Services		
Stakeholder	- LG Franchisor coordinates the operation and collects donation, cooperation with other NGO's and ministries, franchisees are women living in targeted communities.		
Supply Chain	- Franchisees recieve a business in a bag package with uniforms and medicine.		
Financing	- Alliance with BRAC which provides microfinance credits for franchisees.		
Compensation	- 20% of the sales		

Project	**Tosepan Pajti (Mexico)**	**Pros**	**Cons**
Business Model	- Indigenous Cooperative	- System build using local structure. - Important social service provided at	- Need for more doctors but impossibility to hire them for
Product	- Pharmacies		
Stakeholder	- Tosepan Pajti as Franchisor in collaboration with local universties		

	and laboratories, women from the cooperative as franchisees willing to invest and use parts of their house for the pharmacy store	low cost.	financial reasons.
Supply Chain	-		
Financing	- 350$ investment with financing help if needed, products delivered on consignment base		
Compensation	- 20% margin		

Project	**Lijjat Papad (India)**	**Pros**	**Cons**
Business Model	- Cooperative Institution	- Manuel in-house production reduces investments costs. - Strong focus on standardization and quality from LP. - Extensive marketing from franchisor. - Work compatible with family roles.	-
Product	- Snacks and consumer products		
Stakeholder	- LP Franchisee owned by indian women of the cooperative, they empower local „sisters" franchisee to work for LP		
Supply Chain	- LP Franchisor provides know-how and goods, sisters produce and sell the goods		
Financing	- Initial deposit that ensure that they pay the goods they sell		
Compensation	- 1,8$ per KG of goods sold		

Project	**Mi Tienda (Mexico)**	**Pros**	**Cons**
Business Model	- Improve supply chain and hence reduce product price.	- Attacks inefficient supply chain management and lowers product prices. - Purchases remain in local town which generates incremental economic benefits. - Diversification of Mi Tienda services and products. -	-
Product	- Supply Chain Management		
Stakeholder	- Mi Tienda as Franchisor in collaboration with local shops in towns of 5k inhabitants		
Supply Chain	- Mi Tienda provides a central and fast inventory, short term finance credits and good supply chain for the local jobs hence reducing the costs of products		
Financing	- Franchisees join program for free but need to increase purchases at Mi Tienda		
Compensation	- Mi Tienda makes margin on all purchases		