



**UNIVERSITY OF  
STIRLING**

The Role of International Franchises in the Economic Development of Saudi  
Arabia

By

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A Thesis submitted to the University of Stirling for the degree of Doctor of  
Philosophy in Marketing

January 2019

## **Declaration**

I announce that this dissertation has not been previously submitted for any other degree. I further announce that this dissertation contains my own, independent work and investigation. Finally, I hereby give my permission for this thesis to be photocopied.

Signed

Abdulaziz Alotaibi

January 2019

## **Dedication**

This dissertation is devoted to Allah, the most Beneficent and the most Merciful, who helped me and guided me to accomplish my study. This thesis is also dedicated to my family for their endless prayers, support and love and encouragement.

## **Acknowledgments**

I would like to express my sincere thanks and deep gratitude to my supervisor Steve Burt for his guidance, valuable feedback, patience and encouragement along the journey. I also would like to thank the interviewees of the companies that I conducted the interview with (directors, CEOs, General Managers and Operations Managers etc.) who agreed to participate directly in this study and for giving up their time for the interview. I would like to express my thanks to the Saudi Cultural Mission in London for their support to pursue my academic study in the University of Stirling .I would also like to thank my family for their unlimited support to finish my Ph.D. Journey.

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## **Abstract**

According to official sources the Saudi economy, its demographics and customer purchasing power render it an appealing market for the franchising industry. With a population of about 31 million people, there exists a craving for entrepreneurial activities by the younger generation. Franchising as business model, has witnessed tremendous growth in recent times, supposedly generating employment, technology transfer and contributing to revenue, among other effects. Surprisingly, this tempo has not been matched by scholarly interest and investigation into the true contributions and attendant barriers associated with international franchising in the Kingdom. This study intends to fill this void.

The study has a national outlook and seeks to explore the appropriate franchise models in the context of an emerging market such as Saudi Arabia in single sector (restaurants). Through primary and secondary methods of data collection, semi-structured interviews were adopted to fulfil the study's aims and objectives. The researcher interviewed 45 people to explore the appropriate franchise models within the context of the Saudi Arabian restaurants sector and to investigate the potential barriers that may impede the success of international franchising in Saudi Arabia. The information yielded by this study will assist the government in taking appropriate policy measures to enhance the performance and benefits of franchising in the economy. Furthermore, the study is significant in terms of theory building regarding the use of different organisational forms specifically the franchise model in a developing economy. Much of the theories about franchising have been derived from the western developed economies particularly the United States. This study, therefore, extends the body of knowledge on franchising in the developing economy, especially in an Islamic country such as Saudi Arabia.

The findings of the study revealed that pure franchising is appropriate organisational form to penetrate Saudi Arabia in the restaurant sector. International franchising is a vital vehicle for developing SMEs and encouraging the entrepreneurial spirit among Saudi businessmen. The findings demonstrated that SMES benefited from international franchising in terms of improving their management skills and enhancing innovation among SME owners in the restaurant sector. However, international franchising had limited impact technology transfer and providing jobs in



the restaurant sector. Surprisingly, this study identifies that culture and religion are not major barriers to the international franchisor. In contrast, the lack of intellectual property protection and the absence of franchising law appeared to be barriers. The applicability of agency theory in the context of Saudi Arabia has been examined. As a result, payment of royalty fees, franchisee's experience and business development plans, controlling, monitoring and asymmetry of information are the most significant issues that confront the potential franchisor that plans to enter the Saudi market.

**Key words.** Small and Medium Enterprises, International Franchising, Saudi Arabia, Agency Theory, Restaurant Sector, Franchising Roles, Barriers, Organizational Form.

## **Chapter 1: Introduction**

### **1.1 Background to the Study**

#### ***1.1.1 The Development of the Saudi Economy***

Oil was found in Saudi Arabia during the 1930s, and Saudi has since grown into the world's largest producer and exporter of petroleum, having the second-largest proven reserves in the world (Thompson et al., 2012). As a result of the abundance of oil, Saudi's economy has been on a continuous path of transformation and development, which makes the country one of the fastest growing economies in the world. However, this transformation, mostly predicated on a limited resource, has not naturally progressed like most developing nations. The Kingdom's quick rise and huge wealth have been built largely without a sustainable foundation, and unless Saudi Arabia's leadership can find ways to decrease its dependency on oil-based products and services, the country will eventually lose 90% of their petroleum-based export revenues. Therefore, developing sustainable strategies to diversify the Saudi economy is a crucial and immediate mission of the government. Furthermore, oil prices continuously fluctuate in response to global economic and political changes. Such a change, for example, occurred in 2014 with the slowdown of oil prices and the slowdown of China's economy, which is the second-biggest oil consumer in the globe. The decrease in oil price and earnings negatively impacted Saudi's economy. The plunge of the oil price in 2014 led to a decrease of US \$ 100 billion (about 13%) in Saudi Arabia's GDP and a reduction of 10.7% in its stock market index in mid-2014. Further, owing to this oil price shock, Saudi Arabia's public deficit went up to 16% of the GDP in 2015, which impacted the government's spendings. Consequently, public debt in Saudi Arabia sharply increased from 1.6% of the GDP in 2014 to 14.1% in 2016 (Jawadi et al., 2018).

Following the painful experience of the decline in the price of oil and its impact on the economy, the rationale and urgency of economic diversification became much clearer to Gulf Cooperation Council (GCC) governments. They were now seeking to reduce their dependence on oil, long before their oil resources are due to run out, in order to limit the effect of oil price fluctuations on their economies. As a result of the plunging of the oil price, Saudi Arabia was confronted with the significant challenge of finding alternative financial and development projects, which are

contained in a new economic transformation programme, Saudi Vision 2030. This local development programme stresses the importance of diversifying Saudi Arabia's economy by implementing various measures, such as selling 49% of the main oil company, Aramco, to private businessmen in 2018; reshuffling and adjusting economic and accounting systems to enhance the business environment; promoting Islamic banking by applying the Islamic principle of moderation; privatising some government services and creating a range of digital services to improve their quality and other features. In general, the goal of this national programme is to accomplish a complete transformation of Saudi Arabia's economy through structural changes and reforms, which requires more transparency and deep changes from the Saudi government (Jawadi et al., 2018).

According to the Mackenzie Global Institute (2015), the Saudi economy has grown from the 27th largest in the world in 2003 to become the 19th largest in 2014 due to the increase of oil prices. Its GDP doubled, and household income rose by 75%. Further, 1.7 million jobs were created for Saudis, which included a growing number of jobs for Saudi women. The nominal GDP of the country is about \$ 750 billion, which is larger than even Switzerland or Sweden. The Saudi government heavily invested in education, health, and infrastructure and cultivated reserves amounting to almost 100% of the GDP in 2014. However, the Kingdom can no longer rely on their oil funds in order to meet the public spending and overcome the effects of the oil glut, which was caused by the change in the global energy market and a demographic change that will increase the unemployment rate. The participation of Saudi workers is 41%, and productivity has increased to 0.8% from 2003 to 2013; this is much lower than that of many transition economies. In addition, more than half the Kingdom's population is younger than 25 and, by 2030, the number of Saudis aged 15 years and over will increase by about six million .To meet this bulge the government needs to create almost three times as many jobs for Saudis as the Kingdom that been created during the 2003–2013 period.

### ***1.1.2 The Growth of Franchising in the Saudi Economy***

Most scholars reported a positive contribution of international franchising to local markets (e.g., Preble and Hoffman, 1995; Alon and Welsh, 2001; Welsh and Alon, 2001) (see Table 1).

Franchising can add to economic growth and economic development in various ways, such as through job creation, provision of certain basic merchandise and services and extension of a country's tax base. For example, Kaufmann and Leibenstein (1988) claim that franchising can lead to economic growth, particularly in the services sector, due to the lack of efficiency in the emerging market, which is lower as compared to that of the developed world. It can also occur due to the international investors' lack of interest in investing in a developing market. Preble and Hoffman (1995) mention that decision makers in the government have realised the role of international franchises in an emerging market; thus, they improved and developed this model of business. In 1993, twenty-four countries created business associates who focused on franchising, and there are approximately fifty-five local and domestic franchise associations (International Franchise Association, 2004). Franchising is considered a means for economic development in developing economies and for connecting these emerging market to the international market. Alon (2001) mentions the role of international franchising in reducing the unemployment rate. For example, Kodak hired 5,556 workers in China. However, Alon (2004) argued that the parent company of the franchise business may need to restructure their strategy and business plan. For example, Kodak restructured its strategy, and numerous outlets were shut down. A study conducted in Africa measured that for every \$ 5,000 of spending by a franchisor, one position is created (Siggel, Maisonneuve, and Fortin, 2003).

According to the 2015 report published by Spanish Association of Franchisors in Spain, there were 1,199 trade names at the end of 2014 that had a total of 63,869 stores, of which 19,250 were private outlets and 44,619 franchised outlets. According to these statistics, franchising created 159,822 jobs through franchised stores and 89,092 jobs through possess stores in 2014. In France, there are 1,658 franchisors and 65,059 franchised outlets, which hire 323,497 individuals and have a turnover of more than 50,680 million euros (Ferreira, 2016). In Egypt, the number of jobs provided in the franchising sector is estimated to be 45,012, with a development scale of about 24% over the previous two years (Unidroit.org, 2016). In the United Kingdom, the statistics of the British Franchise Association indicate that the yearly revenue of franchising in 2015 was 15.1 billion pounds sterling, while more than 621,000 jobs were created, and there was a growth of 14% of business format franchising systems, with a total of 44,200 franchisee-possessed businesses (Thebfa.org, 2015). Kazakhstan, which has over 350 franchises, has started

more than 3000 franchise firms that hire more than 17,000 individuals, and the revenue of the franchising sector achieves one billion dollars a year (Sayabaev et al., 2016). These examples illustrate the rationale of successful franchises in generating jobs and revenue

The franchise sector in the Middle East began expanding after the Gulf War, with numerous American fast-food firms being established. The franchise market is not only restricted to a single sector but also covers automotive services, beauty, laundry services, printing, hotels, logistics, medical, retail, furniture and restaurants (Ali, 2008). The significance of franchising becomes apparent by visiting any of the commercial districts throughout Saudi Arabia, which are lined with popular western restaurants, clothing stores and other retail outlets. Since the days of the oil boom, Saudi Arabia has been a destination for international franchisors, and Saudi now hosts more than 300 franchises that are operated by foreign companies. The presence of large number of international franchises indicate that the domestic franchises are not developed which show the lack of capability of local SMEs to grow in Saudi Arabia.

Franchising has grown in the past decades and continues to grow in the largest country in the Gulf. There is an expected 10–20% annual growth in the franchise sector, and the paid fees and royalties have exceeded \$ 323 million. The most prevalent franchises in Saudi Arabia revolve around the food and beverage sector, with Starbucks, McDonald's, Burger King, KFC and Subway leading the way, while Gap, Victoria's Secret and H&M are other well-known retail brands. Franchising opportunities in Saudi Arabia are not limited to global brands. The growth of entrepreneurial activity has sparked opportunities for franchising local and regional concepts, which are steadily gaining popularity (Akel and Husein, 2013). The Saudi economy therefore faces challenges in diversifying, away from its dependence on oil. Franchising appears to provide a medium for achieving this, which will also create employment opportunities and develop entrepreneurial skills.

**Table 1. FRANCHISING Chains AND EMPLOYMENT IN Different Developing MARKETS**

| <i>Country</i> | <i>Number of Franchisors</i> | <i>Number of Franchisees</i> | <i>Annual Sales (Millions \$)</i> | <i>Employment</i> |
|----------------|------------------------------|------------------------------|-----------------------------------|-------------------|
| Asia           |                              |                              |                                   |                   |
| China          | 368                          | 3,000                        | NA                                | NA                |
| India          | NA                           | NA                           | NA                                | NA                |
| Indonesia      | 261                          | 2,000                        | NA                                | NA                |
| South Korea    | 1,300                        | 120,000                      | 27,000                            | 530,000           |
| Malaysia       | 225                          | 6,000                        | 5,000                             | 80,000            |
| Philippines    | 500                          | 4,000                        | 105                               | 100,000           |
| Thailand       | 150                          | 3,000                        | 1,300                             | 15,000            |
| Turkey         | NA                           | NA                           | NA                                | NA                |
| Africa         |                              |                              |                                   |                   |
| Egypt          | NA                           | NA                           | NA                                | NA                |
| Zimbabwe       | NA                           | NA                           | NA                                | NA                |
| Europe         |                              |                              |                                   |                   |
| Bulgaria       | 18                           | NA                           | NA                                | NA                |
| Czech Republic | NA                           | NA                           | NA                                | NA                |
| Hungary        | 250                          | 5,000                        | NA                                | 100,000           |
| Romania        | NA                           | NA                           | NA                                | NA                |
| Russia         | 50                           | 300                          | NA                                | 2,000             |
| Ukraine        | NA                           | NA                           | NA                                | NA                |
| The Americas   |                              |                              |                                   |                   |
| Argentina      | 150                          | 1,500                        | 1,100                             | NA                |

|                    |     |        |        |         |
|--------------------|-----|--------|--------|---------|
| Brazil             | 894 | 46,534 | 12,000 | 226,334 |
| Chile              | 50  | 300    | 250    | NA      |
| Colombia           | 80  | 600    | NA     | 11,000  |
| Dominican Republic | 180 | 800    | NA     | 5,000   |
| Ecuador            | NA  | NA     | NA     | NA      |
| Mexico             | 500 | 25,000 | 8,000  | NA      |
| Peru               | 59  | 440    | 375    | 3,250   |
| Uruguay            | 148 | 340    | 360    | 3,600   |
| Venezuela          | NA  | NA     | NA     | NA      |

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Source: International Franchise Association (2003).From (Alon, 2004)

## 1.2 The Study

Surprisingly, despite the phenomenal growth of the franchising business, there are very few empirical studies on franchising in the Kingdom of Saudi Arabia. A literature search yielded only a few scholarly articles, although journalistic articles abound. One scholarly study by Sadi and Henderson (2011) lamented the paucity of franchising studies in the in country. This study seeks to explore the appropriateness of different franchise models within the context of an emerging market such as Saudi Arabia. Many franchisors organise their chains in a “plural form” by having both company-owned outlets or franchised outlets and then manage them as separate lines of business (Bradach and Eccles, 1989). This study also examines the role of international franchising in the development of SMEs, and how international franchises may lead to technology transfer and job creation for the locals. It also seeks to explore the barriers that impede the development of international franchising such as religion, culture and the country regulation system, and the applicability of agency theory within the context of Saudi Arabia from franchisee perspective.

### **1.2.1 Rationale for the Study**

To consider the different franchise models in the context of an emerging market such as Saudi Arabia (specifically in the restaurant sector), and to explore the role of international franchising in the development of SMEs and encouraging an entrepreneurial spirit among local businessmen, it is appropriate to embark on a rigorous study of franchising in the Kingdom. As noted above, previously studies on franchising are limited in scope. Therefore, a more exploratory, detailed and encompassing study is required, which can provide some perspective to inform government policies and improve the management of franchises in general. There is a lack of empirical studies on franchising in Saudi Arabia, which has experienced franchising for more than three decade (Sadi and Al-Fuzai, 2010; Tuncalp, 1991; Al Harbi, 2014; Al-nassar 2010; Jehanzeb, 2015; Sadi and Henderson, 2011; Abughazala, 2006). The Saudi government launched the 2030 vision strategy to move away from oil, reduce the unemployment rate and support the private sector through the growth of SMEs in the KSA. One component of this strategy is to attract international investors to Saudi Arabia and support the private sector to grow by developing small and medium enterprises. In addition, this vision also aims to export local Saudi merchandise to neighbouring countries as well as the rest of the world. Franchising appears to be a key element in this strategy and provides a potential mechanism to deliver the strategy

Previous studies (Sadi and Al-Fuzai, 2010; Sadi and Henderson, 2011) suggest that international franchising is the tool for developing the local SME sector in Saudi Arabia. Looney (2004a), Almobaireek (2009), Otsuki (2002), Merdah and Sadi (2011) and Alharbi (2014) all argue that SMEs in Saudi Arabia tended to fail due to their lack of experience, lack of marketing skills and clear vision; thus, franchising appears to be a suitable means for the Saudi SME sector to overcome its problems. Moreover, the previous studies (Stonehouse et al., 2004; Alon and McKee, 1999; Preble and Hoffman, 1995; Konigsberg, 2008; Alon, 2006) postulated that the master franchise strategy is the most suitable way to enter an emerging market that has a different culture, language and political and economic levels. In 2018, Saudi Arabia hosted ‘The Saudi International Exhibition for Franchise’ at the Riyadh International Conventions and Exhibitions Centre in order to encourage and support Saudi entrepreneurs. The exhibition is returning to the Kingdom in 2019.



However, in order for international companies to enter the Saudi market and for the local entrepreneurs to grow through international franchises, there is an urgent need to update the relevant information and provide empirical studies because there is no franchise association and a lack of information regarding the franchise industry in the Kingdom. This exploratory study will provide insightful and valuable information to the official government bodies, practitioners, local entrepreneurs and international investors. In 2018, researchers at the Rosenberg International Franchise Centre (RIFC) developed an index that ranks 131 countries according to their attractiveness as international franchise expansion markets for US-based franchises. Saudi Arabia ranks # 20 for market potential even though Saudi Arabia ranks very low when it comes to the legal and regulatory environments # 80 .This study will help to identify market opportunities, obstacles, and predict future improvement in the franchising industry in the kingdom.

### **1.2.2 Aims and Objectives**

#### **Aims of the Research:**

This study aims to explore the appropriateness of different franchise models in the context of emerging market such as Saudi Arabia

#### **Objectives of the Study:**

- To explore the role of international franchising for local SMEs, entrepreneurial development, technology transfer and employment in the restaurant sector of Saudi Arabia
- To determine the obstacles, if any, that may impede the operations of international franchising in Saudi Arabia, such as culture, religion and regulations.
- To explore the applicability of agency theory within the context of Saudi Arabia.

### **1.2.3 Significance of the Study**

This study seeks to explore the appropriateness of different franchise models in the context of emerging market such as Saudi Arabia specifically in the restaurant sector, and explore the role of international franchising in the development of SMEs and the encouragement of entrepreneurial spirit among local businessmen. The study will highlight the barriers, if any, often associated with international franchising in the context of Saudi Arabia. The information yielded by this study should assist the government in implementing appropriate policy measures in order to enhance the performance and benefits of franchising for the economy. This study will help international franchisors evaluate the Saudi market before entering it. In the absence of Saudi franchise laws and a franchise association, the vision 2030 strategy presents a good opportunity for international franchisors to invest in the country. Women are now permitted to drive in Saudi Arabia, which will increase the demand for purchasing cars and present a good opportunity for auto manufacturers to invest in the market. The lifting of the ban on cinema will allow international franchisor the opportunity to invest in this untapped sector. Saudi Arabia is also open for tourism and has started issuing visas for tourists, so there is a chance for the international franchisors to invest in recreation and hospitality sector. There is a huge potential for international investors to invest in the country. The question is what business model and organizational form is most appropriate to take advantage of these changes and opportunities.

In addition, the study is important in terms of theory-building regarding the appropriateness of organisational forms in a developing economy such as Saudi Arabia. Most of the theories on franchising come from developed countries that have a similar culture, religion, regulation and economic standing. This study would, therefore, expand the body of knowledge regarding franchising in an emerging economy and Islamic country such as Saudi Arabia. This study aims to contribute to the knowledge on franchising, particularly from the perspective of an emerging market, as franchising is considered a growing business form that has several economic benefits.

### **1.3 Summary**

This chapter presented the background of the study. The chapter shed light on the development of Saudi economy. It is also identify the challenges that may lead to the lack of economic growth such as the drop of oil prices and the high rate of unemployment faced by the Saudi economy

and sheds light on the importance of international franchising for the Saudi economy in terms of job creation and the growth of SMEs. The chapter illustrated the rationale of the study and how Saudi government try to diversify its economy away from oil by attracting international investors. In addition, this chapter highlight the aim and the objectives of the study .The chapter then discussed the significance of the study and its importance in terms of theory building. The study has a national outlook and seeks to explore appropriate franchising models in the restaurant sector of the economy and investigate the role of international franchising in the development of SMEs and encouraged an entrepreneurial spirit among local businessmen and facilitated technology transfer and job creation and highlighting the potential obstacles, if any, that may be faced by international franchising in the region. The next chapter reviews the literature on franchising in order to identify the issues that may be explored in the regional context.

## **Chapter 2: Literature Review**

### **2.1 Introduction**

In this chapter, the existing literature on the contribution of franchising to economic development has been reviewed. The types of franchising have been discussed in addition to the theoretical frameworks explaining the nature and operations of franchising being reviewed. This chapter presents the key literature on franchising and moves from the general conceptualisation of the franchising concept to the specific consideration of the manner in which franchising contributes to the growth of SMEs and relates to the involved socio-cultural contexts.

### **2.2 The Concept of Franchising**

The concept of franchising goes back to the Middle Ages, when the Catholic Church granting franchises to tax collectors in return for a percentage of their income (Cunill, 2006). The Singer Sewing Machine Company was the first organisation to employ franchising as a means of distributing its products (Cunill, 2006). This form of franchising originated in the United States and gradually moved to other European countries. Initially, franchising focused on three sectors: motor vehicle dealerships, service stations and soft drink bottlers (Welch, 1989). Kaufmann and Dant (1999) define franchising as a type of entrepreneurship where the franchisor, who is the possessor of a business, allows the franchisees to use the business trademark and service in exchange for payment (Watson et al., 2005). This type of collaboration relied upon a team working and sharing information between the two parties – the franchisor and the franchisee (Paswan and Wittmann, 2009).

There are two types of Franchising: product/tradename franchising and business-format franchising. *“Product/trade-name franchising is a distribution system in which suppliers make contracts with dealers to buy or sell products or product lines”* (Falbe and Dandridge, 1992, p. 43). The difference between product/tradename franchising and business-format franchising is that business format franchising provides a process of operation that contains a strategic plan for progress and continuous support (Falbe and Dandridge, 1992). Khan (2016) claimed that

business format franchising is the most common and is used in the fast food industry. This type provides the franchisee with a proven business format, good training and technical assistance. Moreover, in the restaurant industry, franchising has become a common business model, encouraged primarily by the American-based restaurant brands for their progress into global markets (Alon, 1999). Stern and El-Ansary (1988) mention that the franchisee benefits from the franchisor's initial and continuous services. For example, the initial services include selecting the location, the negotiation of lease and providing financial support, which are accessible to the franchisee before operating the business. The continuous services provide inventory control and centralised data processing, which is available to the franchisee after managing the business. Usha (2010) argued that franchisees, in turn, bring with them a wealth of information regarding the domestic market. This helps the franchise outlets commence operations faster and far more proficiently than if the franchisor had to do alone. In fact, it would be almost impossible for a franchisor to gauge how the domestic market operates. Affes (2016) states that the American franchisors are interested in penetrating international markets based on three factors: the existence of a middle-class consumer, a stable business environment and a local investor who's interested in their product/service. Franchising is well established business that benefited both franchisee and franchisor to accomplish their mutual goal. The franchisee benefited from the franchisor expertise whereas franchisor benefited from franchisee local knowledge.

The British Franchise Association (BFA) defines franchising as *'a contractual license granted by the franchisor to the franchisee which allows the franchisee to carry on during the period of the franchise a particular business belonging to the franchisor; it obliges the franchisor to provide the franchisee with assistance during the period of the franchise to pay fees'* (Mendelsohn, 1999). In addition, Burton and Cross (1995, p.136, cited in Alon, 2006) define international franchising as *'a foreign market entry mode that involves a relationship between the entrant (the franchisor) and a host country entity, in which the former transfers, under contract, a business package (or format), which it has developed and owns, to the latter'*. In addition, the European Franchise Federation (EFF) defines franchising as *'a system of on-going collaboration between legally and financially separate and independent undertakings, the franchisor and its individual franchisees, whereby the franchisor grants its individual franchisee the right, and imposes the obligation, to conduct a business in accordance with the franchisor's concept'* (Monroy and Alzola, 2005, p. 586).

### **2.2.1 The Franchise Contracts**

The boundary of the franchisor-franchisee relationship is shaped by a contract, which is typically valid from 3 to 20 years. Franchising contracts determine which products are to be sold, the quality standards, prices and hours of operation, and they also specify the start-up date, the duration of the contract, periods of renewal and termination clauses. Franchising is distinctive as compared to other forms of entrepreneurial activity, in that it legitimately elaborates the symbiosis and distinguishes between economic types. Monroy and Alzola (2005) stated that the relationship between the franchisor and franchisee can be seen as beneficial, where the principals transfer their expertise to the agents. Fulop (2000) suggested that a franchisor who handles transactional roles in the franchise system in a professional manner stimulates the success of the system and enhances the performance of the partner. In all business sectors, an agency relationship involves two parties: the principal and the agent. There will always be some misalignment between the interests of the principal and the agent. The principal delegates work to an agent because the principal does not have the skills or resources to undertake an activity. The principal requires the agent to act in his best interest, but the agent's self-interest may dictate otherwise (Anderson, 1984). Franchise relationships are successful when the partners recognise the competence introduced in the relationship, which will lead to enhanced value. Stephenson and House (1971) found that, for franchise relationships, the advantages lie in the potential for bigger profits through teamwork rather than through operating individually. According to Hunt and Nevin (1974), franchisee collaboration may be encouraged by exercising the power to control the franchisee's behaviour or by persuading the franchisee using the potential advantages to be obtained from the relationship. Teamworking and responsibility enhance the relationship between the franchisee and franchisor and lead to the success of the franchise business.

The franchising system format relies on a contractual agreement between the principal and the agent. The agreement between the two parties will allow the franchisee to use the franchisor's brand name under specific standards (Barkoff and Selden, 2008). The contract has two sections. The first requires the franchisee to pay the initial fees to the franchisor for the entirety of the contract. The second part of the contract requires the franchisee to pay royalty fees, which is a fixed percentage of sales (Lafontaine, 1991; Ozanne and Hunt, 1971). The percentage of the

royalty fees is estimated to be about 5–8% of the total gross sales (Daszkowski, 2010). The payment of royalty helps both parties avoid uncertainty regarding the success of the outlet. Rubin (1978) argued that, if the franchisee pays only the initial fees the franchisor, the franchisor will not get the chance to share the success of the business in case things go better than expected.

Caves and Murphy (1976) define a franchise agreement as a contract lasting for a definite or indefinite period of time, in which the owner of a protected trademark grants the right to operate under said trademark for the purpose of producing or distributing a product or service. An agency relationship involves one party (the franchisor) delegating work to another (the franchisee) that undertakes the work (Eisenhardt, 1989a). Rewards and insurance are essential for principals under an agent-theoretic premise. Thus, the franchisors' efforts must align sales with the level of incentives provided to the franchisee (Lafontaine and Slade, 1997). The contractual agreement between the participants in a franchise system is recognised as the formal control mechanism, suggesting goal congruence and providing monitoring capabilities (Eisenhardt, 1989a; Leblebici and Shalley, 1996). The contract is very important to regulate the relationship between franchisee and franchisor especially in conducting business in another country with a different culture.

### **2.2.2 Franchising as a mode of Internationalisation**

There are five main types of strategy for penetrating new markets – master franchising, joint venture, licencing, direct investment and direct franchising. Recent research has found master franchises to be the most common alternative for entering new markets (Welch, 1990; McIntyre et al., 1991; Goncalves and Duarte, 1994).

- **Master franchising:** Christiansen and Walker (1990) define master franchising as where the franchisor allows the franchisee the right to give sub-franchises within an exclusive territory and period of time. The national partner is familiar with the host country's culture and marketing conditions, which aids the international franchisors in coping with language- and culture-based obstacles and country regulations. The local partner is therefore seen not only as a source of revenue for the firm but also as a source of information regarding the aspects of the marketing programme that may require alteration

in order to suit the values of the host country. Moreover, master franchising is a contract that permits the agent to be a sub-franchisor, so they will have more freedom in terms of control and can alter the systems as per the local culture (Alon, 2006a). Kaufmann (1992) mentioned that, in master franchising, the franchisor grants a franchisee the rights to operate multiple outlets from the outset. Area development agreements are a type of master franchising that expects the master franchisee to launch and run multiple outlets within a geographical region according to a specified timetable. Multi-unit franchising is distinct from single-unit franchising in that franchisees run more than one outlet. There are many different forms of MUF. Incremental or sequential MUF happens when a single unit franchisee within a flourishing business is granted and awarded additional outlets based upon the performance of existing outlets. Singular units are managed by the employee manager's employees through the master franchisee (Kaufmann and Dant, 1996).

- **A joint venture agreement:** These arise when the franchisor is interested in partnering with the foreign franchisee in the host country. However, the franchisee is not eligible to grant a sub-franchise network with an exclusive region. The benefit of having a joint venture is that both the franchisor and the franchisee are required to invest in the international business activities. This is an advantage because numerous countries require local equity injection to obtain government permission and because other methods of franchising may not be permitted in the country (Chan and Justis, 1990).
- **Licensing:** The franchisee usually benefits from the technical or business knowledge of the franchisor in exchange of a royalty fee. In return, the franchisor is provided the opportunity to enter a foreign market at little or no risk. (Chan and Justis, 1990).
- **Direct investment:** The franchisor contributes money to firm-owned stores in international markets. This requires the franchisor to provide all of the money and resources needed for establishing the outlets. According to Quinn (1998), the use of company-owned outlets are a means for international franchisors to test the franchise package and the market before expanding to a full franchising basis.
- **Direct franchising:** The franchisor directly establishes and operates individual franchisees in the global market from their home market. Quinn (1998) concluded that this strategy often requires a franchise 'packet', which is carefully chosen to fit the



particular country involved; however, running the operation's activities from the home market might create issues, especially if the number of outlets have increased.

The success of franchise business is determined by the franchisor ability to choose the most suitable strategy to enter foreign market that has different culture, religion and regulation.

### **2.3 Theoretical Perspectives on Franchising**

According to Wacker (1998), 'Theory' consists of four elements: the explanation of concepts or variables, a domain (the exact setting in which the theory can be implemented), a set of correlations and certain projections. A theory may be seen as a combination of constructs and variables in which constructs are related to each other by propositions and the variables are related to each other by hypotheses (Baccarach, 1989). Handfield and Melnyk (1998) argue that theory is crucial for ensuring the meaningfulness of the gathered data. They claimed it is difficult for the researcher to differentiate between the positive and negative outcomes of a study, and empirical studies will be considered 'data-dredging'. Sutherland (1975) defines a theory as '*an ordered set of assertions about a generic behaviour or structure assumed to hold throughout a significantly broad range of specific instances*' (p. 9). The main purpose of a theory is, therefore, (i) to provide a framework of analysis and reference, (ii) to give clarification regarding how we see the world and (iii) to help and enrich our understanding and provide knowledge about the observed phenomenal. According to Hall and Lindzey (1978), a theory is a way of looking at a certain phenomenon from a specific point of view with particular boundaries that are set and justified. These boundaries are important if meaningful answers to the research questions are to be derived from empirical observations. In addition, the authors claim that one of the main functions of a theory is to prevent the observer from being removed from the inherent complexity of the natural world; as a set of lenses, a theory guides an observer in order to avoid having to focus on all observed events (Hall and Lindzey, 1978). The next section explains the different theoretical frameworks that researchers have used in franchising, and these are discussed in depth in association with the theoretical frameworks that were selected for this study, namely resource-based theory, transaction cost theory and agency theory.

### ***2.3.1 Resource-Based Theory***

Barney (1991) explained that resource-based theory concentrates on the correlation between resources and competitive advantage. Resources that are important (relatively rare and difficult to duplicate) are strategic assets that possess the power to yield a competitive advantage (Amit and Schoemaker, 1993). Edith Penrose was one of the first academics to acknowledge the significance of resources to a company's competitive position (Newbert, 2007). Penrose (1959) claimed that a company's growth, both internally and then externally through merger, acquisition, and diversification, is based on how the company used its resources. These resources can also be the key motivations for an international franchisor's competitive advantage and can add value in the new penetrated market (Jell-Ojobor and Windsperger, 2014). The resources and abilities that provide competitive advantages are often rooted in the franchisor's business model or behaviours; thus, the transmission of such resources across local boundaries is hard, and it is difficult for others to emulate and duplicate (Hoffman et al., 2006). Alon (2006) investigated the decision to employ master franchising from the resource-based point of view and claimed that franchisors that were young, with unknown brand names, little resources, and slight knowledge of global operations, may choose global extension over a master-franchisor. International franchisors with competitive advantage increase their success in global market and they appeal to potential franchisee.

#### ***2.3.1.1 The Resource Scarcity View***

The resource scarcity theory views franchising as an organization's response to a shortage of the necessary resources required for its expansion, such as financial capital, labour capital, managerial talent or local market knowledge (Oxenfeldt and Kelly, 1969; Wang and Altinay, 2008, p. 227). Managerial expertise is usually in short supply given the time required to acquire it and the high acquisition costs (Combs and Ketchen, 1999; Combs et al., 2004), but franchising permits immediate access to management capacity (Brickley and Dark, 1987), especially in cases of second-generation franchising. Mendelsohn (1999) mentions that franchisors and franchisees collaborate because they own complementary assets as the franchisor sees the franchisee as a key source for capital, administrative and entrepreneurial talents and the franchisee is worried about

the business format of the franchisor. However, Mendelsohn (1999) indicates that, as the franchisee gains practical experience, he or she becomes more independent and begins to think that there is no value to be gained from the franchisor. Resource scarcity theory emphasises the role of capitals in franchise relationships (Carney and Gedajlovic, 1991). In the resource scarcity approach, the franchisee provides money for business development, through a fixed fee and a royalty rate (Blair and Kaserman, 1982), at implicit interest rates below the market price (Caves and Murphy, 1976). This suggests that selling franchises is a good way for franchisor to overcome their financial and managerial constraints.

Michael (2014) claimed that franchising brings established, tested business **practices** and know-how to the foreign market. Oxenfeld and Kelly (1969) argue that franchising permits rapid market penetration in the early stages of company development by increasing access to key resources. The authors agreed that penetrating the international market helps the franchisor gain capital and knowledge regarding the market through the local franchisee when the franchisee runs an approved business that is associated with lower risk. Moreover, new businesses often lack the capacity to nurture managerial skills and may lack domestic knowledge regarding the markets wherein they are aiming to expand (Shane, 1996a). Franchising provides an important resolution to both of these issues by broadening the scope beyond the limits of the company and charging the franchisee with much of the hazard that is characteristic of introducing new products in new markets (Kaufmann and Dant, 1999).

For Norton (1988), the central characteristic of franchise organisations is that they are a combination of market-like and firm-like qualities. A franchise is market-like due to the trade that exists between the company and its franchisees. The franchisee pays a set amount in order to acquire the right to market the franchisor's products and pays royalties that include a percentage of sales as well. Further, they may be required to purchase specific inputs from the franchisor. The firm-like qualities are found in the manner in which the franchisor's and franchisee's relationship resembles a nearly full vertical integration but with the franchisor exercising significant control over the franchisee. Also, the relationship resembles a contract between employer and employee, in that the contract usually strictly specifies performance criteria and the right of the franchisor to unilaterally terminate their relationship (Rubin, 1978).

In addition, Oxenfeldt and Kelly (1969) explain that franchising is an attractive option because of the franchisee's need for a ready supply of management labour and talent. Shane (1996b) found that it is essential for new firms to overcome the limitations of their resources through a franchising system. However, Oxenfeldt and Kelly (1968), Carney and Gedajlovic (1991) and Shane (1996b) argue that expanding firms through franchising allows access to scarce capital (the franchisees capital) in a cost-effective manner. Selling franchises may therefore be the more cost-effective and realistic option (Dant and Kaufmann, 2003). Furthermore, franchisees may be able to provide capital to the franchisor at a lower cost as compared to passive investors (Combs and Ketchen, 1999). The significance of acquiring franchise is the benefit of training and receiving competence skills (Price, 1993b; Choo and Bowley, 2007; Khan, 2016)

On the other hand, Rubin (1978) suggests that it is not the lack of capital or management resources that fully explains the reason behind firms choosing to franchise. The franchisor's experience helps franchisees be more creative and innovative when running their businesses. Castrogiovanni et al. (2006) claimed that resource scarcity theory assists Small and Medium Enterprises (SMEs) to expand rapidly. Franchising is a favourable option for SME business expansion (Keating, 1989; Sanghavi, 1998). Franchising is seen as a method for reducing the financial and managerial restraints on the development of small- to medium-sized firms and transferring hazards from the company to the franchisee (Oxenfeldt and Thompson, 1969; Hunt, 1972; Caves and Murphy, 1976). Both franchisee and franchisor are benefited from the business model to overcome their challenges and accomplish their goals.

### ***2.3.1.2 The Capital Constraints View and the Managerial–Constraints View***

The capital market imperfection argument is amongst the earliest explanations for franchising (Oxenfeldt and Kelly, 1968; Oxenfeldt and Thompson, 1969; Caves and Murphy, 1976). Franchisees are perceived by the franchisor as a means of dealing with the dilemma of scarce capital, including labour. International franchising helps transfer knowledge, technology, and human capital, enhance the performance and skills of the employees in the workplace, perform technology transfer through being a 'learning organization' and improving the staff performance and abilities such as hardware and machinery learning. This occurs through (1) operating

abilities, (2) investment abilities and (3) innovative abilities (Stanworth, Price, and Purdy, 2001). Combs and Castrogiovanni (1994), Combs and Ketchen (1999) and Combs et al. (2006) show the benefits of the franchise system to be the degree of strategic flexibility and control provided by this form of organisation, which saves on recruiting, training and monitoring costs, and the benefits and opportunities for development arising from having less pressure on money and other incomes. In addition, Peterson and Dan (1990) noted that individuals who chose to become franchisees most valued the business training they received from the franchisors, the relative independence and the advantages of an established business name in comparison to the risks and rewards associated with starting an independent business.

A life-cycle model of franchising was devised by Oxenfeldt and Kelly (1968), whereby in the start-up phases, when there may be a shortage of funds for expansion, the franchisee's capital is used to expand the company. Markland and Furst (1974) have proposed a franchise portfolio optimisation model that can be utilised by potential franchisees to formulate their optimum portfolio. This model has two primary attributes. First, a probabilistic capital budgeting technique is used to evaluate potential franchisees; second, integer programming determines the optimum portfolio of discrete, alternative franchisees based on the rationing of capital and the constraints of the involved risks.

Thompson (1992) found that company ownership is less likely to occur when units necessitate high capital investment. The fact that new franchisors charge a higher initial fee than more established franchisors indicates that resources are important in the early stages of a firm's growth (Sen, 1993). Although it has been widely accepted among researchers, the capital constraint explanation seems to be in disagreement with the theory of finance (Rubin, 1978). In addition, Rubin (1978) uses the theory of portfolio management to emphasise the typically greater risk aversion of franchisees and suggests that there is a higher cost of capital for franchisees.

Oxenfeldt and Kelley's (1968) approach to franchising is to explain its essential nature and prospects and to identify factors that cause franchisors to buy out franchisees. According to Woll (1968), a prospective franchisor considers options over the variety of sources of income that will offer consistent growth of franchisees in the system. The author recognised eight basic areas

from which franchisors gain income. Among these are the initial franchise fee, royalties and the rental of property, the sale or leasing of equipment, raw materials and supplies, the sale of franchise products and the sale of territory rights. In an empirical study, Hunt (1973) found that successful franchise systems are destined to become wholly owned chains, gradually displacing franchisee-owned units but never becoming 100% company-owned. The author identified six basic reasons as to why companies seek to repurchase the franchised outlets, namely the lack of money, issues with franchising principals, the craving for global expansion, separated outlets and inadequate franchise fees. This shows that franchising is a way for franchisor to overcome the financial burden. However, buying franchise outlets could be seen as an opportunistic behaviour by franchisor.

In their study, Zeller, Archabal and Brown (1980) also found the existence of an inclination for franchisors to purchase the more profitable franchisees. In addition, Caves and Murphy (1976) suggest that franchisors must balance the potential income from a shift to company ownership against the investment costs of repurchasing the franchise. According to Lafontaine (1992), 79% of franchisors indicate that they are running at or above their perceived optimum proportion of the income of the company-owned outlets. Oxenfeldt and Kelly (1968) found that the most successful franchise systems eventually become entirely company-owned and that franchising is most advantageous for the franchisor during the early life-cycle stages. Franchising becomes less and less attractive as the company matures beyond the expansion phase and as its goals, opportunities and resources evolve.

### ***2.3.2 Transaction Cost Theory***

According to the transaction cost theory (Williamson, 1975, 1985), environmental uncertainty influences the contract structure as a governance framework. Transaction costs occur due to bounded rationality in a difficult and shifting environment, leading to high environmental uncertainty. Environmental uncertainty prevents the franchisor from detailing in-depth contract conditions and enhances the need for ex-post adjustments by delivering decision rights. Environmental uncertainty requires the adjustment of the franchise business model as per the national environment but also decreases the aptitude of the franchisor to assess the political, economic and sociocultural situation of its operation (Jell-Ojobor and Windsperger, 2014).

Baena and Cerviño (2014) argued that political unpredictability inhibits the international franchisor from penetrating new markets because of the associated dangers.

Based on the information processing view of the organisation (Simon, 1947; Williamson, 1975), higher environmental uncertainty, due to the franchisor's insufficient knowledge to assess the sociocultural, economic and institutional peculiarities of host countries, requires more local information processing capacity by delegating coordination tasks to local partners. Hence, franchisors can effectively reduce the challenges of environmental uncertainty in host countries by transferring residual control rights to the local partner.

Environmental uncertainty in the foreign markets increases the firm's ex ante and ex post transaction costs, especially the search, information processing and adaptation costs (e.g., Williamson, 1991). Environmental uncertainty can be divided into three components, i.e. institutional uncertainty (e.g., Alon, 2006c; Williamson, 1991), economic uncertainty (e.g., Alon, 2006c; Kor et al., 2008; Sánchez-Peinado and Pla-Barber, 2006) and cultural uncertainty (e.g., Alon, 2006c; Contractor and Kundu, 1998a; Contractor and Kundu, 1998b; Erramilli et al., 2002; Fladmoe-Lindquist and Jacque, 1995; Julian and Castrogiovanni, 1995; Kedia et al., 1994; Quinn, 1999; Sashi and Karuppur, 2002). Institutional uncertainty refers to changes in political, regulatory and judicial rules and policies. Economic uncertainty refers to the unpredictability of the demand and competition in the host country, and cultural uncertainty results from the lack of knowledge of the foreign culture (Miller, 1992; Miller, 1993), such as gender roles, ideology, religion and work ethic, language, business practices (Hennart et al., 1998). The lack of institutional infrastructure and the change of the economic policy such as taxation system of international market present threat to franchisor business and increase the transaction cost.

According to transaction cost theory, specific investments result in quasi-rents that can be expropriated by the less dependent partner (Williamson, 1985; Klein et al., 1978). In franchising, both the franchisor and the franchisee have to undertake high transaction-specific investments that increase bilateral dependency (Windsperger, 1994). When the franchisor's and franchisee's specific investments result in high quasi-rents, they are likely to exceed the potential hold-up gained from opportunistic behaviour, thereby increasing the self-enforcing range of contracts

(Klein, 1996; Klein and Murphy, 1997). Lafontaine (1992) mentions that the franchisee is more vulnerable than the franchisor because of the unpredictable success of the business; thus, the franchisor should decrease the initial fees and increase the royalties. The author argued that this will lower the franchisee's risk in case the business does not succeed. Some of the academic scholars (Blair and Kaserman, 1982; Rubin, 1978, 1990) insisted that the franchisor should lower the royalty fees to motivate the franchisee to take care of the business. For example, if the business' brand-name reputation dwindles, it will lead to the reduction of the royalty fees, which affects the franchisor's income. The franchising business model has high success rate compared to running independent business however, there is no guarantee that the franchise business will succeed abroad.

### ***2.3.3 Agency Theory***

Alchian and Demstz (1972), Ross (1973), Jensen and Meckling (1976) and Fama and Jensen (1983) are the creators of the agency theory. The agency theory is an essential component of corporate governance research (Jensen and Meckling, 1976; Fama and Jensen, 1983; Schleifer and Vishny, 1997). In addition, agency theory has been employed in various aspects of more general business research, such as budget control (Demski and Feltham, 1978), retail sales compensation (Eisenhardt, 1988), international joint venture formation (Reuer and Miller, 1997) and supplier-distributor relationships (Lassar and Kerr, 1997). Agency theory has also been used to explain local franchising (Rubin, 1978; Mathewson and Winter, 1985; Brickley and Dark, 1987) and the internationalisation of US franchise systems (Shane, 1996b).

The agency theory, also called the 'principal agent theory' (Alon, Ni, and Wang, 2012), mentions that an agency relationship exists between a franchisor (the principal) and the franchisee (the agent). Agency costs are diminished by increased monitoring or providing greater rewards for the franchise network partner. Doherty and Quinn (1999) postulated that the agency theory is based on the concept of the principal-agent relationship. In this relationship, principals represent individuals, or groups of individuals, who are in control of a set of economic functions or assets through some form of ownership or property rights. The principals have delegated the



day-to-day control of these functions or assets to agents, who operate them on their behalf (Jensen and Meckling, 1976).

Agency theory has been recognised to be helpful in examining franchising as a business form in the international context, with studies revealing that franchise firms are inclined towards raising the number of franchised stores as they become more global (Hoffman et al., 2016). Garg and Rasheed (2003) claimed that international franchisors preferred multi-unit franchising (MUF) because it addresses agency problems, such as bonding, adverse selection, information flow, shirking, inefficient risk-bearing, free-riding and quasi-rent appropriation, better than single-unit franchising (SUF) in the global context. For instance, Dant and Nasr (1998) mention that multi-unit franchises prefer to share information with the franchisor to a greater extent than SUF because they need to maintain the brand-name capital, and they (MUF) are also less likely to engage in opportunistic behaviour, such as shirking, free-riding and under-investing. Although residual clemency and monitoring are considering means for eliminating agency issues (Eisenhardt, 1988; Jensen, 1983; Shane, 1996a), their possible effectiveness in the context of franchising is unsatisfactory. Dant and Nasr (1998) have emphasised that the alignment of incentives, through residual clemency, is difficult to accomplish because the franchisee and the franchisor have different perspectives. These differences cause disagreements between franchisors and franchisees.

Agency issues start to occur when the franchisor is unable to predict what the franchisee is achieving (Kersi et al., 2013). Elango (2007) states that principals who are looking to penetrate the international market should possess the skills to anticipate and alleviate possible opportunistic behaviour by the agents. Quinn and Doherty (2000) argued that the franchisor's experience may assist them in choosing the right franchisees (Sashi and Karuppur, 2002; Doherty, 2009). This is because, through time, principals become more experienced and gain specific know-how (Shane, 1996b). This occurs due to their contact and interaction with the agents on a daily basis (Mariz-Pérez and García-Álvarez, 2009). Mullner, Bernardi Glattz and Schnedlitz (2003) mentioned that the negligence and lack of accountability and knowledge of the franchisee could lead to franchisee bankruptcy. McCosker (1995) and Mendelsohn (1999) also supported this fact and added that franchisees who cannot

follow and adapt to the business formula established by the franchisor are those who are at a greater risk of not achieving success. Sometimes, the franchisee might develop the attitude of a *'maverick'* and become a non-conformist, thus disrupting the franchise chain (Miranda, 1995). McCosker (1995) and Mendelsohn (1999) claimed that providing bad service to the consumer may lead to the franchisee being unsuccessful, even if the franchise's business is well-established. Even though a franchise is an established business and support is always delivered by the franchisor, the franchisee's abilities and skill in terms of controlling the business professionally remain the most vital elements for preventing failure. This includes the capability to retain good financial reports, capability to accomplish aims, capability to cope with management dilemmas and adequate planning during establishment (Mullner, Bernardi-Glantz and Schnedlitz, 2003).

Sometimes, the lack of franchisor experience could lead to the failure of the business. According to the International Franchise Association (2015), the franchisee makes their decision to choose the franchisor's brand based on the franchisor's experience, which includes technical abilities and operational competence. In addition, Combs et al. (2003) and Alon (2001) mentioned that the experience of the franchisor is an important factor that influences the franchisee's decision to choose to run the franchise business. Stanworth (1995) claims that a lack of initial investment by the prospective franchisor could negatively impact the success of the franchise business in terms of both price and time. The author argued that the potential franchisor should dedicate at least two years to developing the business plan and test it. Price (1996) insists that there is a need for a pilot franchise that will help the franchisor. The agents require support, and the franchisor must ensure they are equipped with the resources required to improve the performance of the franchisees. For example, Alon and Alami (2010) mentioned two factors that led to the success of McDonald's restaurants as compared to the failure of Subway in Morocco. The first being that McDonald's has 15 more years of experience in expanding abroad than Subway. The second factor is that McDonald's is present in more than 120 countries, far more than Subway, which is present in 72 countries. The franchisor experience is the main component of the franchise business

In agency theory, franchisors have two basic tools to ensure franchisee cooperation – direct observation of franchisee behaviour, such as monitoring, and the provision of incentives and

motivation to franchisee outputs (Castrogiovanni et al., 2006). Soriano (2005) stated that the agency theory suggests that franchisors aim to reduce their organisational monitoring costs in particular by rewarding a franchisee's efficiency with profits. In addition, Doherty and Quinn (2000) explain that there are two methods through which the franchisor can control the behaviour of the franchisee – coercive and non-coercive control. In this case, the franchise contract functions as the major source of coercive power. According to Doherty and Quinn (2000, p. 358), 'In the franchise context, coercive power includes a set of monitoring systems to ensure strict adherence to the franchise agreement and protection of the franchise trademark. Non-coercive power is obtained through the franchisor's support activities and is concerned with management by persuasion and example, rather than by threat.' Even though the franchisees have autonomy, they are managed by the franchisor, who limits their independence in order to shield the brand name from harm and make sure that the franchisees' objectives align with the organisation's strategy.

The alliance between the two parties, franchisor and franchisees, creates an issue for the company's network strategy (Lawrence and Kaufmann, 2011). In order for the franchisor to exercise managerial control, they should pay attention to the franchisees' need for being independence; this plays a crucial role in encouraging the franchisees to take care of the business (Dant and Nasr, 1998) and makes them more creative. However, Cochet et al. (2008) argued that excessive independence for franchisees can cause the agency cost dilemmas that damage the network's brand name. This confrontation usually occurs due to the conflict caused by the franchisor's desire to maintain power and continue network constancy and the franchisees' need for more independent and ability to be more creative and innovative (Altinay and Wang, 2006). McCosker (1995) and Mendelsohn (1999) demonstrated that a franchise business relies on having a trustworthy relationship between franchisor and franchisee. The franchisee licence may be suspended or not be renewed once the contract expires or in case conflicts have occurred between the two parties. According to Mullner, Bernardi-Glantz and Schnedlitz (2003), the lack of communication and cooperation and the different perspectives of the franchisor and franchisee would lead to disagreement between the two parties that, in turn, would cause the franchisee to fail.

There is an obvious correlation between control and innovation that creates contradiction, as innovation requires freedom (Freije and Enkel, 2007). Housden (1984) mentions that the principal may control the agent's ability to fulfil the demand of the domestic market by controlling marketing variables such as advertising, promotion and territory. Previous academic studies (Knight, 1984; Ayling, 1987; Withane, 1991) insisted that agents worry about the restrictions enforced on them and their inability to make a decision. Agents feel like they do not have the chance to participate in shaping the company strategy because of the lack of autonomy they receive from the franchisors, which limits their entrepreneurial skills.

Felstead (1994) focuses on the inclination towards control being integrated into the corporation and the franchisor exercising this power in order to accomplish their aims. The franchisor-franchisee relationship can be characterised as having four stages. First, the introduction, where mutual inter-reliance provides the same drive for progress and income is generated (Justis and Judd, 1989). The second stage can be categorised as increase, which starts when the business is performing. During this stage, the franchisor provides aid to the new franchisee, and the relationship flourishes and grows. Also, during this stage, the relationship can seem problematic if the franchisor does not provide appropriate training or assistance. When each member is clear regarding what is expected from the other, it can be said that the maturity stage has been reached. The franchisee has a precise understanding of the high quality and expertise of the franchisor and may either value or question the franchisor's contributions to the relationship (Justis and Judd, 1989). The last phase is that of decline. In this stage, either one or two instances occur. The first is that of the business not doing well and the franchisee is driven to end the relationship, and the second is that of the business flourishing and the relationship with the franchisor being solidified (Justis and Judd, 1989). In the franchise distribution system, the majority of the power is controlled by the franchisor instead of the franchisee (Ozanne and Hunt, 1971; El-Ansary and Stern, 1972; Lusch, 1976). This may be explained in part by the bias of the contract towards the franchisor (Forward and Fulop, 1993). Placing condition and terms in the contract could lead to conflict issue.

According to Kidwell et al. (2007), issues that lead to free riding in the franchisor-franchisee relationship are centralisation, formalisation, interaction and external competition. For example, Morrison (1996) argued that in the contractual relationship, each partner has the responsibility of

ensuring that the financial contentment suits both parties and that the franchisee experiences job satisfaction. Klein (1980) claimed that potential franchisees have sufficient time to examine the franchisor's contract and the company's past to determine the number of outlets that have been previously terminated. Franchisors may be reluctant and not favour the dismissal of the business without reason because this action may prevent prospective franchisees to become involved in the franchise business. The franchisor has the right to dismiss franchisees; however, the franchisor should provide support and help to the franchisees who free-ride in order to retain the strength and save the reputation of the brand (Brickley et al., 1991a). The level of transparency and sharing information for both franchisee and franchisor is very important for relationship prosperity.

Agency problems have also been classified as vertical and horizontal problems. Vertical agency problems relate to the confrontations that occur between the company and the store bosses. Rubin (1978) argues that franchisees are superior to employees as a solution to the vertical agency problem of motivating outlet managers, as franchising provides the franchisee manager with all the profits after expenses (Fama and Jensen, 1983). Franchisees do not shirk because their income is tied to their effort. Employee managers, in contrast, will shirk because they do not possess strong ownership incentives (Rubin, 1978). Accordingly, their behaviours must be monitored closely, which is expensive (Bradach, 1997). Thus, resolving the vertical agency problem requires a trade-off between monitoring and incentives. Having a good relationship with restaurants managers is essential for reducing the monitoring cost and eliminating the opportunistic behaviours.

Although franchising reduces monitoring costs, certain vertical agency problems remain because the potential for opportunistic behaviours, such as shirking, is two-sided (Lafontaine, 1992). Storholm and Scheuing (1994) itemise several possibilities for opportunism by both parties. Franchisors can (a) place outlets too close together, (b) terminate the franchisee in order to reopen a franchisor-owned outlet at the same location, (c) force franchisees to purchase inputs from the franchisor, (d) misappropriate advertising royalties and (e) design the franchise contract in a manner that favours the franchisor during disputes. Franchisees can hurt the franchisor by (a) releasing the franchisor's proprietary information, (b) failing to pay royalties and (c) not adhering to quality standards (Combs, Michael, and Castrogiovanni, 2004). Huszagh et al. (1992)

claimed that franchisors with a bigger and mature chain have a better monitoring ability and are able to travel globally. Aydin and Kacker (1990) concluded that companies that prefer not to expand their business abroad thought that they are not competent and do not have the basic resources to manage their business. In addition, Shane (1996b) indicated that monitoring experience and the franchisee's capability to run the franchise affected the franchisor's decision to go global. Fladmoe-Lindquist and Jacque (1995) investigated 10,000 separate locations of 12 US franchisors operating globally to determine the factors that influenced the franchisor's decision to run or to franchise in that specific location. Franchisor would find it difficult to monitor outlets in countries that are geographically different from the US. In addition, the high cost of advertising hinders the franchisor's inclination to franchise. The long distance (Location) between countries and culture dissimilarity increase monitoring cost. Franchising is preferred where monitoring is costly (Combs, Michael, and Castrogiovanni, 2004).

Horizontal agency problems refer to the potential for franchisees to free-ride on other outlets, as all outlets operate under a shared brand name and customers transfer goodwill associated with one outlet to others (Brickley and Dark, 1987; Caves and Murphy, 1976). Certain investments that the franchisees make in the brand yield spill-over benefits for other franchisees. Carney and Gedajlovic (1991) point out the following agency problems in franchise relationships: inefficient investment, free-riding and quasi-rent appropriation. Inefficient investment results from the fact that franchisees have a large proportion of their wealth tied up in one or a few units, and they therefore have to consider the full risk of each of their marginal investments. The problem of free-riding refers to the situation where the franchisee attempts to cut costs by offering a lower quality than specified by the franchisor. In these cases, the franchisee benefits from the system's well-known brand name but incurs lower costs as compared to the other franchisees. As a result, the franchisee's lower quality offerings might damage the reputation of the franchise system. The free-rider problem is particularly common in franchises with few or no repeat customers (Brickley et al., 1991). The third agency problem is related to the issue of quasi-rent appropriation. A quasi-rent exists if the value of an asset is higher in its current form of use than in its alternative uses. Quasi-rents arise when partners make relation-specific investments (Carney and Gedajlovic, 1991).

However, principals are constrained by the entrepreneurial capacity dilemma (Norton, 1988); they do not have enough time for monitoring and devising control systems. The costs of obtaining information in order to pay attention to the agents, and the costs of negotiating and applying incentive mechanisms, constitute the agency costs in a given relationship (Fama and Jensen, 1983). In implanting agency theory to franchising, researchers have argued that creating a new outlet leads to a critical dilemma for chain organisations. Thus, the firm and its owner are faced with choosing an agent to run the outlet – they can rely upon a company-owned unit with a salaried manager or an external franchisee who is allowed to retain the unit's profits in return for a fee. In both cases, the delegation of responsibility incurs agency costs. These costs are often assumed to be higher in company-owned units where salaried managerial labour encourages *'shirking and the excessive consumption of leisure'* (Rubin, 1978, p. 226). Nevertheless, the interests of franchisors and franchisees are not perfectly aligned, as franchising also creates incentives for franchisees to free-ride (Castrogiovanni et al., 2006).

For example, the cleanliness of one outlet affects customers' perceptions of all outlets. Since the benefits are shared, franchisees prefer to free-ride on others rather than to invest. These individual decisions potentially lead to chain wide under investment. One solution is implementing increased monitoring by the franchisor; however, doing so undermines a key advantage of franchising, which is that it substitutes incentives for expensive monitoring (Rubin, 1978). Thus, firm ownership is predicted when horizontal agency concerns might lead to under investment (Combs, Michael, and Castrogiovanni, 2004). As Brickley and Dark (1987) argue *'consider the case of a fast food chain restaurant in a location where the probability of repeat sale to a customer is low. In this situation, the franchisee has an incentive to supply lower quality products'*. Outlets vary in their dependence on the shared brand name. Rural locations have proportionally more repeat customers, which assures the franchisees that the returns from investments in quality are captured. Accordingly, rural locations are more likely to be franchised (Brickley and Dark, 1987; Norton, 1988). One empirical problem, however, is that rural locations might be franchised because they are costly to monitor as well as because repeat customers encourage efficient investment. Thus, distinguishing between the effects of monitoring costs (vertical agency) and customer mobility (horizontal agency) proves to be a challenge (Combs, Michael, and Castrogiovanni, 2004). A bad selection of location could also be the factor that leads to franchisee failure (Mullner, Bernardi-Glantz, and Schnedlitz, 2003),

wherein it can affect the product or service that is welcomed by the consumers. Hanson (1995, p. 62) claimed that it is difficult for franchisors to secure property for their franchised sites in Moscow because the mayor controlled most of the property. Choosing the right location is important which require the involvement of the franchisor and keeping the franchisee away from doing free ride or shirking behaviour.

External factors have also been discussed by McCosker (1995) and Mendelsohn (1999) as one of the factors contributing to franchisee failure that is outside the franchisee's power. Examples of such factors include currency devaluation, aggressive and inexpensive rivals, and recession in the economy, government policies and diplomatic relationship between two countries. Opportunism can take the form of adverse selection, where agents initially overstate their abilities to accomplish a task, such as opening and efficiently running a retail establishment (Katz and Owen, 1992). Opportunism also creates the risk of a moral hazard, where the agent, a company-owned outlet manager for example, puts in less than the optimum effort required in order to produce outputs on behalf of the principal. Because of these agency issues, an organisation's principals must find methods to identify and motivate agents to act in ways that are in line with the principal's interests and do so in a cost-effective manner (Eisenhardt, 1989a). The franchisee will reap the rewards of high performance or suffer losses due to poor performance (Katz and Owen, 1992; Kaufmann and Dant, 1996). Porter and Renforth (1978) identify the three most common issues faced by franchisees as cooperative advertising, franchisor inspection and evaluation, and minimum performance requirements. Franchising tie-in contracts can be recognised to eliminate costs that could prevent the franchisee from free-riding on the franchisor's trade name (Klein and Saft, 1985).

Doherty (1998) employing the agency theory perspective emphasises the importance of the information transfer process, the information asymmetry problem and associated controlling costs. She claimed that these factors will influence the retail company's decision to expand globally. Agency theory suggests that in order for international retail franchisors to control their overseas franchise business, they need to implement strict rules in their franchise contract (Lafontaine, 1992; Shane, 1998). The agents who content the performance standards outlined by franchisors in terms of training, start-up, financial and monitoring support tend to acknowledge and appreciate the achievement (Fulop, 2000; Lashley and Morrison, 2000). In addition,



franchisors who perform in the franchise system with a high level of competency will enhance the level of confidence and trust between the two parties, and this helps progress the relationship (Harmon and Griffiths, 2008). Honesty and transparency between the franchisee and franchisor limit the asymmetry of information issue.

Zeller, Archabal and Brown (1980) found that the aims of franchisors and franchisees conflict with one another, in that the franchisor struggles to increase gains for the whole system whereas the franchisee prefers to increase gains within its boundary, particularly the outlet gains. In their study, Doherty and Quinn (1999) argued that information asymmetry becomes an issue in the principal-agent relationship when combined with the moral hazard. Hutchinson (1995) stated that, for large firms whose shares are actively traded on the stock market, this information asymmetry problem recedes in importance. It can, however, remain a significant problem for companies that have large amounts of intangible assets in the forms of brand names, research and development and advertising.

In addition, Doherty (1998) has asserted that the ease or complexity of the information transfer process, with its consequences for the information asymmetry problem, plays a pivotal role in explaining the entry-mode choice of international retailers. For example, where different levels of economic development exist between foreign and domestic markets, where there are differences in retail regulation with regard to employment law, planning regulations and opening hours, and where the internationalising firm's ability to assess the risk of the foreign venture is limited due to these complexities (Doherty, Quinn, 1999). The foreign country regulations and system influence the franchisor decision to determine the entry mode strategy to enter the market.

## **2.4 Franchising in Context**

Franchising, as a business model, can be employed in a variety of contexts. These contexts may add further areas for consideration. Relevant to this study are particular contexts – small and medium business development and the socio-cultural context.

### **2.4.1 Franchising and Small Business Development**

The definition of SMEs is different across the world in terms of the company size, shape and investment level (Darren et al., 2009). The European commission (2012) defined SMEs as organisations that have no more than 250 employees and an annual turnover of less than 50 million euros (Arafat and Ahmed, 2013). In the UK, SMEs are defined based on their turnover and number of employees. A company with a turnover of less than £ 3.26 million and no more than 50 employees is recognized as a small firm, while a firm that has a turnover of up to £ 25.9 million with less than 250 workers is considered a medium-sized company (Statistic of SMEs for the UK and Regions, 2009). Abu Al-faham (2009) has denoted the concept of a small business by noting the capacity of money that is spent in the project. A small business is not expected to invest a substantial amount of money, but the determination of their commitments varies from one country to another. Small businesses are categorised based on the value of its trades. This standard is seen as a trustworthy measure for the level of business activity. Small businesses can be classified as one of the vital drivers of economic growth for any country (Al-Khatib et al., 2015).

Both SMEs and entrepreneurship have a tendency to accomplish the same goal; however, they are different concepts (Darren et al., 2009). They are also known for the important role they play in the socio-political-economic change of the local economy (Rebecca et al., 20029). Rebecca et al. (2009), Okpara et al. (2007) and Ogundele (2007) have stated that issues, such as environment, culture, location, individual characteristics and firm characteristics, influence the growth of both the SMEs and the entrepreneurship. Furthermore, the SME managers and entrepreneurs are inclined to have similar traits in the context of business administration. These traits include resourcefulness, determination, persistence, vision, problem-solving, dedication, honesty and trustworthiness (Rebecca et al., 2009; Ogundele, 2007) (see Table 2).

**Table 2. The difference between Small and Medium Enterprises and Entrepreneurship**

|                | <b>Entrepreneurship</b>   | <b>SMEs</b>  |
|----------------|---|--|
| Definition     | Process where an individual discovers, evaluate, and exploits opportunities independently | Firms or business ventures managed by individual owners  |
| Size           | Large, Medium or Small. Number of people<br>Small to large                                | Small and Medium only Small  |
| Purpose        | To discover, innovate and establish   | To produce, buy and sell   |
| Degree of risk | Varies  | Lower  |
| Sector         | Private, government and not-for-profit  | Private sector only  |
| Key attributes | High need for: achievement; internal control; creativity and innovation; growth           | Organizational skills to manage efficiently, little innovation, moderate growth, moderate need for achievement |
| Growth Focus   | High  | Varies   |

Source: (Darren et al., 2009) cited in (Olusegun, 2012).

Franchising is regarded as a source for small businesses developed either directly through the franchise system or indirectly through associated business relationships in the host market. The important consideration when assessing the importance of franchising to the small business community is that of whether the failure rate of franchisees is lower than that of traditional

independent small businesses (Boe, Ginalska, and Henward, 1987). The franchisor transfers a comprehensive business package to the franchisee, which includes managerial skills and specialist employee training (Stuart and Brownmen, 2001). One statistic exists that claims to prove that franchises has a lower failure rate than self-managing small businesses (Ayling, 1988; Housden, 1983; Ozanne and Hunt, 1971). For example, according to Alon and Banai (2000), McDonald's invested in food-processing factories in Russia for providing meat and vegetables, and the franchisor of Baskin Robbins and Dunkin' Donuts invested more than \$ 40 million, which led to improvement of infrastructure and production factories while providing a good supply chain. Teegan (2000) claimed that franchisors often import key materials of their business from their market. With time, franchisors attempt to obtain or develop national sources for host markets. Mail Boxes Etc., for example, adopt this strategy when they expand abroad; they import key materials from their home market and later obtain national sources (Alon, 2004). Holt (2003) mentions that international franchising eliminates capital flight by offering opportunities to invest in the emerging market.

Overall, franchising provides numerous advantages for the SMEs that are seeking to grow. For franchisees, it provides goodwill associated with the franchise name, access to inexpensive goods and services and professional assistance with operational performances (Zimmerer and Scarborough, 2002; Justis and Judd, 2004). It also provides the ability to choose the correct site (Mendelsohn, 1998; Stern and El-Ansary, 1988), design (Gower, 1995), and staff recruitment and training (Barrow and Golzen, 1990). Furthermore, it embraces purchasing and financial systems, market data, promotional and pricing policies and funding (Barrow and Golzen, 1990). Hunt (1972) evaluated the impact of franchising in the United States when it accounted for only 25% of the total consumer goods' expenditures. One of his key findings was the ability of franchising to stimulate local independent businesses. His study revealed that franchisees believe that they are independent because they control key areas of operations, such as hours of operation, book keeping, advertising, pricing, standards of cleanliness and staffing. Second, 52% reported that franchising was their only potential option for self-employment. Thus, if the experience from the US is any indication of franchising growth in developing countries, franchising has the potential to increase the opportunities for SME development by providing the possibility of business ownership to those who would otherwise not take the risk (Alon, 2004).

In the context of Saudi Arabia, there is no clear definition of SMEs. According to Sivakumar and Sarkar (2012), there are a number of government organisations that use different definitions for SMEs in Saudi Arabia. For example, the Saudi Industrial Development Fund classifies SMEs based on their annual sales, which do not exceed SR 20 million. In addition, commercial banks define small companies based on annual sales, ranging from SR 100 thousand to SR 5 million, and workers, ranging from 2 to 49. Further, they classify medium-sized companies as those that have annual sales of SR 5 million to SR 50 million and 50 to 200 employees (see Table 3).

**Table 3.** The Saudi Arabian General Investment Authority categorises firms based on the number of their employees, as presented below:

| <b>Type of enterprise</b> | <b>Number of employees</b> |
|---------------------------|----------------------------|
| Small-Size Enterprises    | Less than 59               |
| Medium-Size Enterprises   | 60–99                      |
| Large-Scale Companies     | More than 100              |

Source: (Mohammad, 2015)

Al-Qahtani (1433, AH<sup>1</sup>) claimed that small businesses are important for economic development, as they contribute to the country’s national income. Small businesses aid in increasing value creation and add to the balance of payments by reducing imports. In addition, the development of small businesses help the country substitute imported goods with yielded local products, which promotes the growth of the export sector of the nation. The small businesses are considered catalysts for increasing the managerial, technical, productive and marketing capabilities that help

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<sup>1</sup> The publisher of the article used the Islamic calendar.

individuals run their business. Saudi Arabia has recognised the importance of supporting SMEs, stating its objectives clearly in its Vision 2030. Under the Saudi Vision 2030, the country intends to raise the contribution of SMEs to the GDP from the current 20% to 35% by easing their funding ability and motivating commercial banks to allocate up to 20% (currently 5%) of the overall loans to them. The government also plans to cultivate talent with skills to encourage the SMEs sector within Vision 2030 in order to cut the unemployment rate from 11.6% to 7% and raise female participation in the labour market from 22% to 30%. One of the important steps in assisting these firms was that of setting up the General Authority for Small and Medium Enterprises in 2015, which plans to enhance the SME contribution to the economy from 500 billion Riyals in 2014 to 2 trillion Riyals in 2030 (Jureidini, 2017). The development of private sector through supporting SMEs contribute to the national economy.

Zamperi (2012) found the main hindrances faced by SMEs owners in Saudi Arabia are the difficulties associated with gaining financial support, bureaucracy, lack of credit options as well as the unfriendly business environment, inadequate government support, unpredictable policy changes and lack of training. In a study conducted by Hassan (2006) mentioned that SMEs in Saudi Arabia have difficulty in obtaining bank loans because their products and services do not align with international standards. Moreover, the author stressed that SMEs lack marketing skills. For example, the people who own the company do not generate feasibility reports, retain proper financial records or possess the ability to prepare annual budgets for their firms.

Additionally, Ramady (2010) mentioned that the Saudi government focuses on the petrochemicals and manufacturing sectors. These industries acquired sizeable subsidies in order to develop the Saudi economy, which led to the neglecting of SMEs. Furthermore, Sugair (2002) claimed that the majority of SME managers are expatriates who had short-term employment contracts and visa constraints, leading to the lack of development of the sector in the long run. Looney (2004a) claims that owners of SMEs in the KSA struggle with the lack of training and thus limit their trading to the local market instead of expanding to the global market. For example, in a survey of 60 existing SMEs in a particular province of the KSA in the year 2000, over 75% reported issues with marketing. The firms in Saudi Arabia require marketing know-how in order to have success with their local and global operations (Kavoossi 1995; Al-Aali, 1995; Al-Zamel, 1993; Leonidou, 1996b; Yavas, 1997).

The reason for the failure of SMEs in Saudi Arabia is associated with a couple of factors that are related to the owner's insufficient management performance, difficulty in obtaining well-experienced staff, absence of sufficient training, absence of creativity and creation of new products and difficulty in finding people who specialise in marketing (Almobaireek ,2009; Merdah and Said ,2011) . Otsuki (2002) identified the obstacles faced by medium and small companies in Saudi Arabia in several areas, including lack of money, lack of qualified human efficiency, lack of management skills for owners of these companies, lack of specialists in marketing skills, lack of availability of technology, special problems regarding the high cost of purchasing materials and the absence of a competent authority to provide information about the Saudi markets. The lack of capability of SMEs present a threat to the development of private sector.

Franchising has been seen as a growth tool for SMEs development and job creation in Saudi Arabia (Sadi et al., 2011; Sadi and Henderson, 2011; Sadi and Al Fuzi, 2010).Franchised SMEs in the wholesale and retail, real estate and restaurants and hotel industries employ large numbers of individuals, which comprises over 60% of the respective workforces. About 540,000 proprietorships are involved, and franchising makes up 35% of family owned SMEs (SAMA, 2003). Revenues are also substantial, growing at an annual rate of 10% in the case of local franchises, which constitute 60% of the total; the remainder is dominated by American and European companies (US-Saudi Arabian Business Council, 2003). Franchised businesses are dispersed throughout Saudi Arabia, but 75% of SME franchises are found in the Eastern Province, Riyadh, Mecca and Medina areas (Malik, 2004; Radwan, 2002; Sugair, 2002), where consumer purchasing power is highest. This suggests that there is a strong relationship between the development of national economy and international franchising.

#### **2.4.4 Franchising and the Socio-Cultural Context**

Webster (1994) defines culture as *'the ideas, customs and skills of a people or group, that are transferred, communicated, or passed along to other generations'*. Hall (1976) stated that there is a difference between 'high' and 'low' culture in terms of interaction and communication. For example, in a low-context culture, such as that of the United States, communication is carried out

in clear terms that are documented or verbally expressed in the same manner as their intended meaning. Whereas, in a high-context culture, such as that of the Middle East communication is included in the physical context, which leads to words not being expressed in the same manner that they are intended (Keegan and Green, 2000). Johansson (2000) claims that people in the Gulf States are believed to come from a high-context culture, in which context affects meaning. High-context cultures are inclined to communicate more on non-oral levels as compared to low-context cultures, where the use of words have greater meaning than the context. High-context cultures tend to be more homogeneous than low context cultures. These cultures are also more fatalistic as compared to low-context cultures. Citizens with high levels of fatalism do not think that they have much control over incidents that affect them and believe such incidents to be managed by destiny (Raven and Welsh, 2004). In Arab cultures, where Islam is the dominant religion, fatalism is characterised by the phrase ‘insha’ Allah’, which translates to ‘if God wills it’ (Rice, 1999). Deresky (2008) mentioned that relations in Saudi Arabia are more informal and communication is implicit (informal relations are considered as an important tool for business activities in Saudi Arabia and other gulf countries (Tyeb, 2003). Paying attention to the cultural differences between countries need to be take into consideration before penetrating the market.

Fladmoe-Lindquist (1996) postulated that in order for international franchisors to succeed, they are required to adapt their standards as per the national culture of the host country. A person’s food preferences and eating habits are related to the culture with which a person is affiliated; these preferences and habits cannot be changed easily (Kitter and Sucher, 2008). Moreover, Hodgetts and Luthans (2003) stressed that franchisor organisations have to alter their business models in order to adhere to the norm and local culture of the host country. However, Contractor and Kundu (1998a) argue that, due to the cultural distance between the franchisor and franchisee market, international franchisors possess the right to protect the standardisation of their product and the business’ brand image. Moreover, Buckley and Casson (1998) claimed that international franchisors have the right to run their business in a manner that they believe will protect their brand and standards, which will in turn meet the international customers’ expectations. Standardisation helps reduce the costs of the raw materials and of controlling the franchisee (Kaufmann and Eroglu, 1999). The level of adaptation differs from one culture to another. For



example, Countries with similar culture may require little adaptation compared to country with dissimilar culture.

Scholars in marketing and sociology (Levitt, 1983; Sklair, 1991) have suggested that the world is being increasingly populated by cosmopolitan consumers, whose tastes and desires are becoming standardised. Advances in technology and communications, international trade and investment and the movement of people and ideas drive these global commonalities across nations.

Comparing the cultural environments facing global franchising in 1988 and 2000, Kaufmann (2001) noted that, although cultural differences exist, they are fast disappearing due to the advances in technology, international broadcasting, commercial messages and global brands. Leonidou (1996a) claimed that Japanese products that are sold in Gulf States differ a little or moderately from the ones sold in the Japanese market. The progress of technology and exposure through traveling limit the cost of adaptation.

Fladmoe-Lindquist (1996) indicated that implementing tough standardisation by franchisor organisations impeded the progress of the franchising business. In addition, numerous international franchisees have different cultures and business environments, which encourage adaptation to meet the market demand (Cox and Mason, 2007). Kaufmann and Eroglu (1999) argue that national franchisees who follow the international franchisor's standardisation without alteration based on their local market demands might struggle from a lack of profitability. Adaptation is important to ensure acceptable standards in terms of running the franchise system and customer satisfaction as compared to rivals engaged in the same business (Narver and Slater, 1990). Elzeiny and Cliquet (2013) examine the difference in service quality between different McDonald's fast-food franchise outlets. The study found that McDonald's did not succeed in providing a similar standard in terms of service quality through dissimilar countries, particularly in Middle Eastern countries such as Egypt. Standardization is difficult to implement especially if the foreign market's culture (consumer behaviour, taste and habits) differs from the franchisor's native country. Flexibility and mutual understanding is needed between the franchisor and franchisee which will reflect on franchise business growth.

Adaptation to the franchisor's standards may be required in order to fulfil the franchisee's national market (Garg et al., 2005). Principals implement standardisation to ensure the smoothness of the business and ensure that the agent adheres to the company rules in terms of product quality and service (Baucus et al., 1996). However, due to the high cost of controlling franchise activities, the franchisor can implement certain levels of control that might lead to mistakes and hiring issues (Dant and Gundlach, 1999). Stonehouse et al. (2004) mentioned that following strict standardisation by the international franchisor could cause problems for the host country's culture. Moreover, Harrison et al. (2000) stressed that it is extremely important for international companies to adjust to the issues that are sensitive to host country norms and religions. For instance, in France, McDonald's introduced beer, while Pizza Inn had to add fish as toppings on its pizzas in Russia (Bucher, 1999). In addition, in Japan, McDonald's turned its attention to the young generation instead of focusing on the older generation in order to promote the brand, as it was difficult for the company to alter the eating habits of the latter (Chan and Justis, 1990). These arguments signify the importance of adapting to the local culture

Adjustment is crucial because customer preferences vary across geographic locations and over time, and failure to adjust to such shifts can lead to lower performance (Szulanski, Jensen, and Lee, 2003; Castrogiovanni, Justis, and Julian, 1993; Yin and Zajac, 2004). Franchisees raise adjustment issues because their knowledge of the domestic market provides them with insight into the associated preferences, and their ownership position drives them to act on this knowledge (e.g., Kidwell and Nygaard, 2011). In an effort to respond to the domestic tastes that vary based on national preferences, franchisees often alter product and service characteristics such as pricing, operating hours and operational routines (Darr, Argote, and Epple, 1995; Lafontaine, 1999). Yin and Zajac (2004), for example, illustrated how franchisees assisted a pizza chain in adjusting to domestic market variations and enhanced its operation by integrating dine-in and delivery services wherever appropriate. Franchisees can also help franchisors deliver innovation that can enhance productivity and prevent chain-wide maturity (Kaufmann and Eroglu, 1998). The authors noted the importance of the franchisee's knowledge for the franchisor, which helps them adjust their brand to suit the local culture and thereby avoid failure. For example, the American franchisor of McDonald's asked the Japanese franchisee to follow the same location strategy as that used for the American McDonald's restaurants, which targeted

the suburban areas because of the importance of drive-through sales (Love, 1995). However, the Japanese franchisee recommended that the restaurants be opened in urban areas based on their high population density. Ultimately, the location strategy suggested by the Japanese's franchisee succeeded (Love, 1995). This signifies the importance of the local knowledge of the franchisee which saves time on doing research and cost saving.

A lack of cultural awareness has led many franchisors, even large organisations, to make mistakes in their expansion format (Justis and Judd, 1989; Hoy and Hoy Echegaray, 1994). Frequently, alterations may be necessary not only in the ingredients and menu options but also in operational policies (Sadi, 1994). For entrepreneurs without such expertise, improving their talent for cultural adjustment may be elusive, as it largely relies on personal awareness and an ability and willingness to search for knowledge (Kirzner, 1973). According to Bell (1996, p. 56), the relationship between cultural differences and the choice of entry mode is more complex than is generally assumed. Further, the larger the cultural difference, the larger the problem. Contractor and Kundu (1998a) claimed that adaptation is necessary to an acceptable level, which will help prevent the international franchisors from losing their business standardisation while meeting the host country's needs. Hawkes and Bandyopadhyaya (2000) believed that, due to culture distance, franchisors might face problems caused by the high cost of penetrating new markets, and this might influence the entry mode strategy. Marketing research is an important tool that needs to be taken into consideration before entering a new market which helps in choosing the right strategy and reflects on saving costs.

Numerous academic scholars (Alon and Welsh, 2001, 2003; Welsh and Alon, 2001; Sheth and Parvatiyar, 2000; Thompson and Merrilees, 2001; Pine, Zhang, and Qi, 2000) argued that franchisors should stay away from engaging in a consistent business model and consistent marketing strategy. International marketing should not conflict with the host country-based marketing modifications. For example, Subway is also adapting to the Indian market (DeLuca 2002). Due to religious prohibitions against pork (Muslim) and beef (Hindu), Subway uses lamb, chicken and turkey instead of pork or beef in its sandwiches and offers a variety of new vegetarian options. The important aspect for franchise chains to improve upon is monitoring – the

capability to assure quality through several entities in different countries around the globe (Fladmoe-Lindquist, 1996; Fladmoe-Lindquist and Jacque, 1995).

Hoffman and Preble (2004) claimed that international franchisors need to pay attention to the tastes and habits of the national consumers as well as the price. The author claimed that this is the most important socio-cultural issue for international franchisors who choose to expand their business abroad. Welsh et al. (1998) stated that American franchisors should pay attention to Kuwaiti tastes, as the people's taste tends to change; they move from traditional to what is considered new and trendy because Kuwaiti citizens tend to travel and are familiar with the latest fashion trends in Europe and the USA. Hoffman and Preble (2004) found price sensitivity to be an important socio-cultural issue in Egypt due to the low GDP per capita. The authors emphasised the importance of franchisee knowledge in helping the international franchisor overcome socio-cultural issues in a foreign market. Hoffman and Preble (2004) claimed that the practices of the code of ethics are considered to be an issue for international franchisor who are unfamiliar with the attitude of other nations. Lovett et al. (1999) claimed that honesty and trust in Asia tend to rely more on individual relations than on contract law.

Alon (2004) argued that international franchising has a positive impact on the society and the culture of the host country. International franchising leads to higher standards of living and greater options for customers. International franchising has contributed and increased the degree of female engagement in the workplace in emerging countries. However, Huszagh et al. (1992) argued that the cultural environment for international franchising causes more difficulties for franchising in a host country. A cultural environment that is completely dissimilar from the franchisor's home country not only affects the contract negotiation process (Weiss, 1996) but also raises problems such as personnel, hiring and franchise policy (Justis and Judd, 1989). The franchise idea and its associated management systems are expressions of the cultural basis of the franchisor's country of origin (Huszagh et al., 1992), and the transferability of the system becomes a function of the cultural gap between the foreign and local cultures. Aydin and Kacker (1990) argue that the very strength of the franchise format, and its standardisation, makes its replication in foreign markets successful.

Tuncalp (1991), international franchising leads and enhances the standard of living, provides the consumer with different choices and increases value through fixed prices and good quality products and services. The presence of international franchising in fast food restaurants in Saudi Arabia reduced the stigma associated to eating out. Sadi et al. (2011) postulate that franchising has positively impacted the lifestyles of Saudi citizens and has played an important role in changing their consumer behaviour in the context of product quality and customer loyalty. Most Saudi consumers considered international franchising beneficial for the Saudi culture and society. Even though Saudi Arabia is considered to be one of the most conservative countries in the world, it does not prevent its citizens from enjoying the products of international brand with a touch of western culture. International franchising has a social impact on the national economy through enhancing and improving the life style of the locals.

Jones (2003) mentioned that customer expectations are extremely high, and there is a demand for high-quality brands at low prices. Further, maintain high customer commitment is becoming increasingly difficult for companies. For example, Grünhagen et al. (2010) state that international fast-food franchises have introduced new lifestyles in Egypt. Home delivery has become widespread, and themed parties at international franchises have become a popular way of celebrating birthdays for Egypt's youth. Additionally, community relations activities of many international franchises have helped modernise schools and subsidise local hospitals. Socially, the presence of international restaurants have changed the behaviour of the Egyptian people. For example, hygiene and a high quality of standard have permitted people to feel more comfortable and safe, enabling them to allow their children to go out on their own. Numerous national and global restaurants started fulfilling their responsibility towards the public by donating funds for renovating student facilities and finance hospitals (Fath, 2007).

Michaele (2014) mentions that international franchising can be seen as an educational instrument for teaching reliability, dependability and teamwork. International franchising raises the level of competition, which lowers costs and raises quality and variety. Moreover, international franchises enhance customer well-being, as mentioned by Grünhagen and Witte (2005). For example, customer satisfaction surveys, complaint handling and recovery from a poor service experience and frequent buyer discounts or couponing are all concomitant imports when a

franchise chain begins operations in a developing economy. Franchise outlets in the restaurant sector intend to enhance the criteria of hygiene in preparing food and general sanitation (Watson, 1997). Moreover, it educates customers by providing nutritional information in restaurants chains as well as by providing the benefits of car-repair advertisements that educate the consumer about car maintenance.

However, the presence of the international franchise in the host country may force local companies out of the market and cause ethical issue. For example, the French Associated Press (2001) indicated that French consumers took to the street to protest against a McDonald's franchise they believed to be a threat to their local traditions, which led to French farmers losing their jobs in cheese factories. In addition, they claimed it is an unhealthy choice for their children. Local Egyptian groceries were enjoying a stable market share before the arrival of the British retailer Sainsbury's. The brand's retail strategy is to sell their products at prices that are lower than that of the factories. This strategy appealed to the Egyptian people – both poor and rich – which impacted the sales of independent groceries by lowering their sales to 40%. This put the local groceries in an extremely vulnerable position (Eltahawy, 2000; Huband, 2000; Bryant, 2000; Drummond, 2001).

On the other hand, Assad (2008) claiming that exposure to foreign brands is one of the reasons that led Saudi society to excessive consumption. She sees this as a threat to the social order. In addition, the author mentions that emulating the lifestyles of western society might cause economic, environmental, social, psychological and health problems in Saudi Arabia. Alturki et al. (2018) argued that the presence of international fast-food chains in Saudi Arabia led to unhealthy habits and obesity in Saudi children.

Religion is an important factor that international franchisors need to pay attention to once they decide to penetrate an international market. Understanding the influence of religion is essential because social norms are known to have a strong impact on human behaviour (Sunstein, 1996; Cialdini and Goldstein, 2004). Previous studies argued that religion is a key social mechanism for controlling beliefs and behaviours (Kennedy and Lawton, 1998). Islam has no issue with the Western view of entrepreneurship as an economic activity, but strongly argues that an economic

activity must be based on ethical and moral foundations and be socially acceptable, just like all other activities (Al Habtoor, 2001; Siddiqi, 1979).

Milliken (1987) states that sensitivity is an important concept that is meant to explain the relationship between establishments and their environment. Friedman (1985) claimed that the components of religious sensitivity are the boycotting of Western goods and halal credibility problems that led to consumers boycotting certain products in the market. Jackson and Schantz (1993) stated that more than 300 market boycotts were planned and executed. In 2003, numerous organisations and their goods were boycotted. Among the fast food brands that were boycotted were American- and Israeli-made products, such as McDonald's, Kentucky Fried Chicken, Pizza Hut and many more (Knudsen et al., 2008). Boycotts of American fast-food chains in Arab countries have been launched by those who want to protest against America's support for Israel. Due to these calls for boycotts, Burger King was forced to withdraw its Whoppers from a food court in an Israeli settlement in the West Bank. Burger King was then denounced by pro-Israel groups in the USA. The McDonald's franchise in Saudi Arabia announced that 26 cents would be donated to Palestinian children's hospitals from each burger that was sold (Balisunet, 2009). In general, boycotting is considered an issue for the international franchisor, especially in countries where religion is a sensitive topic such as Saudi Arabia.

### **2.4.3 The Research Gap**

Existing theory justifies strategic preferences between market- or hierarchy-based organizational forms by concentrating on how the characteristics of an exchange decide the most efficient form of organization (e.g., Williamson, 1991). Yet companies frequently establish an exchange employing both market- and hierarchical-based organizational form even when technology and market segments are apparently the same (Bradach and Eccles, 1989; Parmigiani, 2007). When applied to business-format franchising, this preference for a plural form of organizing happens when a franchisor has a combination of both company-owned units and franchisee-owned units. A significant number of companies that run franchise systems also operate their own units; e.g., McDonald's corporation has about 20% company-owned units (6,815) and 80% franchised units (24,624), and Hilton Hotels has about 55% company owned outlets (293) and 45% franchised units (231). (International Franchise Association, 2009a, 2009b). This study seeks to explore the

most appropriate franchise models in the context of emerging markets such as Saudi Arabia, specifically in the restaurant sector, and explore the role of international franchising in the development of SMEs and in encouraging an entrepreneurial spirit among local businessmen to facilitate technology transfer and job creation . Many international franchisors are becoming interested in emerging markets because Western markets have reached saturation and the competition has increased, which has reduced revenue (Alon and Mckee, 1999).

Welsh et al. (2006) suggest that more empirical research needs to be conducted on all aspects of franchising in emerging markets, and the differences between these countries and regions should be examined while taking into consideration the role played by governments in organising franchise environments in these markets. There are few empirical studies that explored the role of international franchising in developing countries (Falbe and Dandridge, 1991; Alon, 2001; Micheal 2014; Sanghavi 2001; Welsh, 2006; Alon and welsh, 2001; Welsh and Alon, 2001; Grunhagen and witt, 2005; Preble and Hoffman, 1995).A number of authors, both industry analysts and academics, have identified emerging markets as a topic that requires further research (Kaufmann and Leibenstein, 1988). A systematic review of 126 empirical studies of franchising found that these studies came from 17 countries; the majority of these studies were performed in North America and the United Kingdom (67%), while the rest were conducted in Europe (17%). There were only seven empirical studies carried out in Asia (Nijmeijer et al., 2013). Young McIntyre and Green (2000) investigated the content of the articles released by the international society of franchising through their proceedings. Out of the 70 articles released between 1987 and 1999, 9 dealt with economies that were in transition and 14 dealt with emerging economies.

Consequently, the majority of franchising research is based on one country's experience – the US. Over the last two decades, the subject of franchising in developing economies has appealed to researchers to conduct empirical studies in the Mexican, South American and Asian markets (Singapore, Malaysia, Hong Kong, Indonesia) (Welsh et al., 2006). According to Welsh, Alon and Falbe (2006), emerging markets, which account for 80% of the world's population and 60% of the world's natural resources, present massive, potential business opportunities for international franchisors. The US Department of Commerce estimated that over 75% of the



expected growth in world trade over the next two decades will come from emerging countries, particularly big emerging economies, which account for over half the world's population but only 25% of its gross domestic product (GDP). About 96% of the world's population resides outside the US, which has the biggest economy in the globe (Elango, 2007).

Alon and McKee (1999) mentioned that, in the last twenty years, academic scholars have focused on franchising's opportunities and challenges in the US and Europe. Previous studies on international franchising have focused mainly on entry strategies (e.g., Agarwal and Ramaswami, 1992). Quinn and Doherty (2000) and Doherty (2007) indicated that there is a need to investigate the field of franchising from an international perspective. The literature on franchising has examined topics such as why companies engage in franchising, and the relationship between franchisor and franchisee. In contrast, international franchising has garnered inadequate academic attention (Quinn and Doherty, 2000; Doherty, 2007).

In general there is a lack of franchising research that has been carried out regarding the Saudi franchising sector. There is currently no clear data available to allow the monitoring of the performance or the direction of the franchise industry in Saudi Arabia. There are a lack of academic studies on the Saudi franchise sector. Although Saudi Arabia owns 60% of all Gulf State franchises (Alnassar, 2010), the field of franchising research remains unexplored (Tuncalp, 1991; Abughazala, 2006; Sadi and Al-Fuzai, 2010; Sadi et al., 2011; Alharbi, 2014; Sadi and Henderson, 2011). Alharbi (2014) conducted a systemic review of previous studies on franchising in MENA countries (see Table 4). According to this review, the majority of these studies adopted quantitative approaches, focusing on one region – the East Province of Saudi Arabia. However, Alharbi (2014) stressed the need to conduct more qualitative studies in different franchise sectors in order to better understand the development of the franchise business in the MENA countries particularly in Saudi Arabia, and each country needs to be examined and tested separately.

*'Unfortunately, there is very limited academic research on franchise development in countries such as Saudi Arabia. Most of the literature is written in the business field and takes the form of books or magazine articles'*

(Maritz et al., 2007).

**Table 4. Published journal articles about franchising in MENA regions**

| <b>Country</b>            | <b>Authors</b>           | <b>Main aspect</b>  | <b>Industry</b> | <b>Main results</b>  |
|---------------------------|--------------------------|---|-----------------|--|
| Egypt                     | Gru'nhagen et al. (2010) | Consumer agency of U.S. franchises                                  | Fast food       | (+;-) U.S. fast food consequences  |
| Egypt                     | Elsaman (2012)           | Model of combination of U.S., Chinese, and Malaysian franchise laws | Not described   | Proposed a legal framework to regulate franchises  |
| Morocco                   | Alon and Alami (2010)    | Comparison of U.S. franchise strategies used in the Moroccan market | Fast food       | Framework for guiding international fast food companies  |
| Morocco, Algeria, Tunisia | Chanut et al. (2013)     | Institutional Theory  | Not described   | (+) Moroccan market more preferable for franchising  |
| United Arab Emirates      | Briggs and Araghi (2009) | Use of commercial agency law  | Not described   | (-) Commercial agency law does not differentiate between franchise, agency, distribution contract and franchising agreements |
| Kuwait                    | Welsh et al. (1996)      | Management effects  | Retail          | Essential managerial skills of sales personnel   |

|              |                           |  |               |  |
|--------------|---------------------------|--|---------------|--|
| Saudi Arabia | Tuncalp (1991)            | Franchise problems   | Fast food     | (-) No specific franchise law  |
| Saudi Arabia | Abughazala (2006)         | Mode of entry  | Fast food     | (-) Saudization, limited franchise regulations   |
| Saudi Arabia | Sadi and Al-Fuzai (2010)  | Effectiveness of franchising as a tool for SMEs successes              | Various       | (+) A strong relationship between the perceived benefits of franchising and success of SMEs                            |
| Saudi Arabia | Sadi and Henderson (2011) | The significance of franchising among SMEs in Saudi Arabia             | Various       | (+) Franchising is a suitable and profitable business mode for SMEs in Saudi Arabia but there are some barriers.       |
| Saudi Arabia | Sadi et al. (2011)        | Role of franchising in the success of SMEs from a customer perspective | Not described | (+) Franchising is a beneficial mode for Saudi SMEs to develop while simultaneously enhancing the lifestyles of Saudis |

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Note: '+' indicates a positive effect; '-' indicates a negative effect

Source: (Alharbi, 2014)

Most restaurant chains employ the plural form. Of the largest 100 restaurant chains (in terms of number of entities ) in 1988, 74 had plural forms (i.e., a mixture of company and franchise units), 22 had only company-owned units, and four had only franchised units; among the top 25 chains, 24 had plural forms, and one had only company-owned units (Technomic, 1989). The biggest chains in the restaurant business depended completely on the plural form. However, this type of organizational form, cannot be generalised in Saudi Arabia due to differences in the social, legal, cultural, religious, political, language, economic, purchasing power, population and customer-demand characteristics between Saudi Arabia and other emerging markets. Arab countries cannot be labelled as the same or a similar market but rather as twenty different markets sharing cultural, language, moral and religious beliefs as well as common aims for economic growth (Elbashier and Nicolls, 1983; Dunn, 1979). The reality of Saudi people is different from other Arab regions (Hutchings et al., 2010).

Saudi Arabia is an ultra-conservative country with a high-context culture that implements Sharia law. This distinguishes it from other emerging market such as India, China, Croatia and Brazil. In addition, the presented theories are based on Western culture and developed economies particularly United States. Maritz et al. (2007) claimed that KSA has a conservative and orthodox culture that is different from Western culture. Saudi Arabia has different taxation and regulatory systems. Batra (1997) claimed that previous research on emerging markets has been too general for it to be relatable to certain countries because of the significant difference in consumer incomes, average education levels, transportation and logistical systems, human development and marketing data among the countries. As existing theories and empirical studies are based on other cultures; their applicability in the cultural context of Saudi Arabia is worth investigating.

This study intends to close this gap by exploring the appropriateness of different franchise models that are suitable for the Saudi Arabian restaurant sector. This study also examines the role of an international franchises in Saudi Arabia in terms of SME, entrepreneurial development, job creation and technology transfer to the local market and identify the obstacles that impede the success of an international franchising focusing on the restaurant sector. Sadi and Henderson (2011) stated that more research is needed to explore the manner in which SMEs

grow through franchising within the context of Saudi Arabia and the Middle East. The researcher is interested in the restaurant sector because most of the international brands that have employed the franchising model are in this sector in Saudi Arabia. The main business industries that experience international growth in franchises are restaurants, retailers and services. These are the sectors where franchising has a robust presence (Hoffman and Perble, 2004). Franchising was associated with restaurant sector for a long period of time (Lashley and Morrison, 2000; Sen, 1998).

The current study differs from previous studies (Sadi and Al-Fuzai ,2010; Tuncalp ,1991; Sadi and Henderson,2011; Abughazala,2006) by adopting a qualitative approach to explore the favourite franchising organizational forms in Saudi Arabia. The majority of previous research on franchising in Saudi Arabia focused on a single region (Sadi and Al-Fuzai , 2010; Tuncalp ,1991; Sadi and Henderson,2011) and most of it was carried out by non-Arabic speakers. This study also focuses on the three main major cities of Saudi Arabia (Riyadh, Jeddah and Al-Khobar) where the majority of the franchise businesses are concentrated in. Further, the study relies on multiple sources for data collection, which increases triangulation. The researcher is also a male Saudi citizen. It has been suggested that, in conducting cross-cultural research, insider researchers who share similar social, cultural and language backgrounds are better suited than outsider researchers in terms of speaking the same language as the interviewees, understanding local values, knowledge and taboos, knowing formal and informal power structures, obtaining permission to conduct the research, gaining access to records and facilitating the research process with ease (Liamputtong, 2010; Merriam, 1998).

## **2.5. Summary**

This chapter starts with the definition of the franchising concept using different definitions. The franchising contract between franchisor-franchisee has been discussed. The chapter is also shed light on the type of strategies that can be used to penetrate new market such as master franchising, joint venture and licensing. The chapter reviewed the previous theories on international franchising such as resource-based theory, transaction cost theory, and agency theory. The chapter also reviewed previous studies and literatures on SMEs and the importance

of international franchising for the development of SMEs. The chapter also illustrated the importance of international franchises to the development of SMEs in Saudi Arabia and also shed light on the obstacles that led to the failures of local SMEs such as lack of marketing skills, studying the market and the lack of financial support. In addition, this chapter highlights the socio-cultural impact of entering a new market such as culture , religion and how culture may affect the progress of franchising when it comes to product adaption and modifying the brand to meet the local taste and . Finally, the research gap had been explained and has been justified by researcher. The next chapter review the literature on the Saudi context focusing on economic background and franchising.

## **Chapter 3: The Saudi Arabian Context**

### **3.1 Introduction**

The objective of this chapter is to provide the context for the current study. The chapter begins with a background history of Saudi Arabia and the economic situation of the country. The chapter provides an overview of the role of international franchising on the economy focusing in the restaurant sector. In addition, the entry mode option and issues are discussed along with other related issues that may impede international franchising in Saudi Arabia, such as culture religion and country regulations.

### **3.2 Country Background**

The Kingdom of Saudi Arabia is the largest country in the Middle East. Saudi Arabia has the biggest population among the Gulf countries and, geographically, Saudi Arabia is the 12th largest country in the world (Alkadry, 2015) (see Figure 1). Contemporary Saudi Arabia was established in 1932 under the leadership of King Abdulaziz. The discovery of oil in 1934 helped Saudi Arabia become one of the richest nations on the earth per capita. The revenue generated from the oil sector allowed the new country to develop its economy, infrastructure and education system (Hamden, 2013).

According to Business Monitor International, the country's GDP per capita is forecasted to reach US \$ 28,864 by 2021, which is up from US \$ 23,368 in 2017 and far higher than the MENA regional average of US \$ 8,634 at the end of the forecast period. The upper-middle class, with a household income of US \$ 25,000–50, 000, will continue to be the dominant consumer group and is forecasted to comprise 32.4% of the total households by 2021, which is up from 25.7% (Saudi Arabia Consumer & Retail Report, 2018).



Figure (1). The Geographical Map of Saudi Arabia

Source: (Ishimatsu et al., 2017)

The Saudi economy relies heavily on producing oil and exports for generating income, which is in turn driven by an oversized public sector. The Saudi petroleum sector constitutes about 87% of budget incomes, 42% of the GDP, and 90% of the export profits (IndexMundi, 2018). Saudi Arabia, despite its great wealth from oil production, is considered to be a developing economy based on the GDP per capita and is strongly influenced by its cultural and religious traditions (Idris, 2007). The global index compiler MSCI included Saudi Arabia in the Emerging Market index on 20th June 2018. Also, FTSE Russell has upgraded Saudi Arabia to an emerging market status. However, Dow Jones is still studying to include Saudi Arabia in the emerging market index (Saudi Gazette, 2018).

Despite being the biggest economy in the Middle East in terms of GDP, Saudi Arabia is at risk due to the global oil market change (Wilson, 2008). Saudi Arabia has been going through



economic growth during the last few years. However, in their study, Noland and Pack (2008) claimed that the Saudi government may struggle to provide jobs to its citizens and improve the education system and social reforms of the country in the future because of the drop in the oil market (Raphaeli, 2005; Meijer, 2010). The Saudi government needs to diversify its economy rather than rely on one sector. Therefore, the government needs to take advantage of the oil revenue by investing in its own people, improving education and creating new job opportunities for its growing population. The decrease of oil prices have forced the Saudi government to initiate considerable reforms in order to diversify its economy away from oil, increase the non-oil GDP and encourage the private sector that is controlled by a few big businesses in the services. One of the basic objectives of the Saudi government in its Vision 2030 strategy is to create a well-diversified economy by 2030 (Mensi et al., 2017).

In order for the Saudi economy to lean away from its reliance on oil, the Saudi government should make significant changes in the three fundamental pillars of their economy as '*without change across these three pillars (labour, business regulation and fiscal management), the full potential transformation cannot happen*' (Mackenzie Global Institute, 2015).

Reforming the labour market is important for productivity and developing the skills of Saudi employees. It is crucial for Saudi Arabia to improve its attractiveness for business in order to attract US \$ 4 trillion in investment (Mackenzie Global Institute, 2015) by allowing competition and limiting the bureaucratic process.

According to researchers and demographers, the increasing number of young people in Middle Eastern countries poses economic, political and social challenges for their representative governments. For example, the lack of political and economic vision in neighbouring countries, such as Egypt and Tunisia, has led to numerous young generations protesting against the government. The Kingdom of Saudi Arabia has to be aware of all the challenges that it might face in the near future. These challenges are high unemployment levels among the young citizens, overdependence on foreign workers and the gap between the Saudi curriculum and the needs of the global market. Saudi Arabia suffers from incompetent Saudi employees, which prevents the country from keeping up with advanced technology (Curry and Kadash, 2002).

As a part of its reform, the Saudi government is delivering a localisation policy called a Saudization. Saudization is a progress strategy that aims to replace non-Saudi nationals with Saudis citizens (Looney, 2004b; Al-Dosary and Rahman, 2005), limiting the reliance on foreign workers in the market. The Saudi authorities focus on the private sector in order to create jobs for its citizens (Sutton, 2015; Randeree, 2012). However, the Saudization strategy may face challenges due to the low salaries in the private sector as compared to the public sector. In the September of 2012, the government attempted to force private companies to pay Saudi employees as much as their public companies' counterparts, with the intention of pushing more Saudis to work in the private sector (McDowell, 2012). Iqbal (2010) argued that the Saudi workers are not qualified to meet the needs of the local labour market. The Kingdom heavily relies on the expatriate worker to fulfil technical needs. The reliance has hindered the country's ability to improve and provide qualified Saudi employees in order to coerce the private sector to offer attractive salaries to the Saudi citizens (Al-Kibsi et al., 2007).

The private sector in Saudi Arabia had witnessed resistance to the Saudization attempt (Ramady, 2010). The Saudi citizens prefer to work in the public sector over the private sector because the public sector is believed to offer job security (Al-Ali, 2008). Budhwar and Mellahi (2006) mentioned that it is difficult to fire any citizen from a public sector job. The reluctance of citizens to be employed in the private sector is rooted in the local culture (Alromi, 2001). A study conducted by Alshathry et al. (2014) claimed that culture has a large influence over Saudis' views of organisation desirability. Baqadir (2013) stressed that managers in the manufacturing industry in Saudi Arabia perceived Saudi workers to be unenergetic. For example, Al-Fawzan (2005) mentions that bank clients in Saudi Arabia note that bank workers generally do not possess enough knowledge to answer their inquiries sufficiently, indicating the lack of proper training. The Saudi authorities attempt to give young Saudis access to technical education in order to equip them with the skills required for the job market (Rahman, 2014). However, Varshney (2016) noticed that the mind-set and perception of the younger Saudi population has shifted and they desire to be employed in the private sector or accept any kind of position. The youth of Saudi Arabia is looking for experience as well as looking to improve their career and contribute to the economy.

Saudi Arabia is one of the largest Middle Eastern recipients of foreign direct investment (FDI), which accounted for \$ 16.4 billion and 38.2% of the total Arab FDI inflows for the year 2011. Saudi Arabia consistently topped the list of host countries for inter-Arab FDI over the past 17 years, with an accumulated total value of \$ 47.8 billion and a 27% share of the total inter-Arab FDI for that period. The Saudi government makes a tremendous effort to maintain the flow of FDI by improving the infrastructure system and working to improve the regularity environment (Al Obaid, 2018). However, obstacles remain that confront the inflow of FDI, such as the government intervention in the local context of hiring requirements, lack of legal environment and unfair treatment when it comes to preferring local companies to international ones (Saudi Arabia Trade and Investment Risk Report, 2018).

The Saudi Arabian General Investment Authority (SAGIA), which was founded in April 2000, has an important role in providing information that helps foreign investors (Al Obaid, 2018). The SAGIA intends to attract more international investors into the Kingdom to create jobs for Saudi citizens and bring in new technology in order to boost economic growth. The Saudi government allows international investors 100% percent ownership in the wholesale and retail sectors. (Jureidini, 2015). According to SAIGA, the number of national and international firms launched in Saudi Arabia since the implementation of the international investment law has increased from 820 in 2000 to 6,478 in 2010 across a range of different sectors; however, the chemical, petrochemical and construction sectors contribute more than 30% of the FDI inflow (Albassam, 2015).

### **3.3 Franchising in Saudi Arabia**

Foreign investors have several different options for entering the Saudi market. The options vary from informal contractual relationships to forming a Saudi Arabian company. The methods depend on the type of business activities (U.S Commercial Service, 2015) (see Table 5). In general, most international companies elect to set up a limited-liability company (LLC). Limited-liability companies can be 100% owned by foreigners or have mixed ownership. Licenses should be gained from the Saudi Arabian General Investment Authority (SAGIA) (U.S Commercial Service, 2015). However, international firms may be eligible for tax treatment or other economic

rewards from the Saudi authorities, especially if Saudi businessmen conduct business with the new company's capital. The Saudi government now allows international companies to conduct business in the wholesale and retail sectors, where many franchise firms are found, permitting investors to own as much as 75% of the joint venture. The international firms looking to invest in the Kingdom of Saudi Arabia need to enter a joint venture with a Saudi counterpart. Previously, the equity split was 50-50, but the government decided to increase the foreign franchisors' equity in an attempt to attract more international investors. International franchisors are required to have the name of the brand or the service in order to register the franchise in the Ministry of Commerce. The franchisor needs to be the original owner as third-party ownership is not permitted by law. As per Saudi law, sub-franchises from the Gulf States do not need to be the original owner to register for the franchise unlike foreign franchisors. Registration procedures may take up to 4–6 months. However, despite the changes, the franchising system in Saudi Arabia is still unclear, and many international franchisors may encounter difficulties when they plan to grant a franchise business to their Saudi partners. (Shujauddin, 2009).

**Table 5. The preferred strategies for penetrating the Saudi market.**

| Strategy                                       | Definition   |
|--|--|
| <b>Technical and Scientific Service Office</b> | The office requires a license from the Ministry of Commerce and Industry. This method protects the independence and personal information of the international firm and provides more flexibility in controlling and promoting the firm's goods or services. Technical and scientific service offices are not permitted to link directly or indirectly in commercial activities, but they may provide technical and data support to Saudi distributors as well as provide market surveys and product research.  |
| <b>Branch Office</b>                           | Saudi Arabia's International Investment Law permits foreign firms the possibility of 100% ownership of projects and the property required for the project itself, while allowing them to keep the same incentives provided to local firms. A branch office requires more direct presence than a commercial agent. Branch offices provide administrative roles and may not be involved in trading businesses. International companies can open an independent branch office without a Saudi partner. The parent company must accept full responsibility for all work undertaken by the branch office in Saudi Arabia. |
| <b>Independent Office</b>                      | To establish an independent office in Saudi Arabia, a foreign company needs to provide to Saudi officials a copy of its commercial registration and written approval from the board of directors of the origin company to open a subsidiary office stating the name of the city and the name of the subsidiary's manager.  |
| <b>Liaison Office</b>                          | A liaison office is usually only for firms that have more than one contract with the authorities and requires a local office to oversee contract enforcement. Representative offices are not permitted to be involved in direct or indirect commercial activity in the Kingdom.  |
| <b>Joint Venture</b>                           | A company can start a joint venture with a local Saudi firm. Usually, the Saudi business authority refers to limited liability partnerships as joint ventures. These partnerships must also be registered with the Ministry of Commerce and Industry, and the partners' liabilities are limited to the extent of their investment in the partnership. Finally, foreign companies can acquire a license from the Saudi  |

|  |   |
|--|---|
|  | Arabian General Investment Authority (SAGIA) to set up an industrial or a non-industrial project in Saudi Arabia.   |
| <b>Limited-Liability Companies (LLC)</b> | This is the most common type used by international businessmen in Saudi Arabia. It is easy to start and control, and the personal liability of each partner is limited to the individual partner's involvement in the company's share capital.  |
| <b>Franchising</b>                       | The international franchisor needs to have a local Saudi franchisee and register the franchise. The franchisor must be the original one and may not be a third-country franchisor. All franchise agreements should be in accordance with Saudi Commercial Law and must be approved by the Ministry of Commerce and Industry. A foreign company is strongly recommended to seek advice from lawyers who are familiar with Saudi law before starting the business or changing or terminating a franchise agreement. |
| <b>A joint-stock company</b>             | A joint stock company needs documents from the Minister of Commerce and Industry after evaluation Company's 'feasibility' study. The law requires the through a Royal Decree based on the endorsement of the Council of Ministers for any joint-stock companies with concessions, for undertaking public sector projects, for receiving assistance from the State, in which the State or other public institutions participate, or for joint-stock companies engaging in a banking business.                      |

Source: U.S Commercial Service (2015)

Akel and Husein (2014) examined the Saudi franchising market and found that most foreign investors involved in the services sector in the Saudi market, such as restaurants, maintenance, IT support and other services. The Saudi Arabian General Investment Authority (SAGIA) does not request any minimum paid-up money for a services entity, but it is common for firms to have a minimum capital of 500,000 Saudi Riyals. International investors engaged in retail or wholesale trading are not allowed to form an LLC because the ownership of Saudi citizens must be 25%. The minimum funds requested by the Saudi government for retail or wholesale trading firms is 20 million Saudi Riyals, and the capital of the Saudi stakeholder is exempt from this figure. Another international investment choice is the building of manufacturing premises that

produce goods in Saudi Arabia that will be delivered to national franchisees. A minimum capital of 1 million Saudi Riyals is requested by the Saudi government for establishing such activities.

Khan and Khan (2001) investigated the restaurants industry in the Middle East, paying attention to the success factors related to franchising. The author stressed the political and legal considerations, culture, language, demographics, traditions, economic change, menu items and the accessibility of the resources that the franchisor is required to consider before penetrating the Middle Eastern market. Baena (2011) investigates how market situations may restrain the entry mode option into Middle Eastern countries such as Saudi Arabia. Franchisors should be aware of the political issues in the Middle East; it is a diverse region, and the political situation is extremely heightened (Garten, 1997). The Gulf States are not similar to other Middle Eastern regions (Fletcher and Brown, 2005). Baena (2011) demonstrated the significance of the country's economic growth, corruption and competence in terms of contract implementation to attract international franchisors. The study concluded that franchisors looking to expand their business in countries categorised to have 'low transparency' will choose master franchising. For example, Bershka and Zara, the fashion retail brands, penetrated the Saudi market by signing a contract with the master franchisee Fawaz Alhokair Group, one of the biggest retail groups in the Middle East.

Young (2001) claimed that foreign retailers in the Gulf States have to form a joint venture in which the foreign partner is limited to 49% equity. This may change, however, as the Gulf Cooperation Council members join the WTO. The alternative is to enter into a franchise agreement, although the franchise laws can be complex. Franchising strategy have worked well so far, especially in a region where the demands are influenced by the strictly controlled Islamic societies. It is crucial for international investors to find the proper partner in the Middle East because the gulf investors' value the relationships. They are enthusiastic in terms of bringing shops to their country, and the majority of the gulf investors come from wealthy family-owned companies (Martin, 1999). International companies may have partners for all the Middle Eastern countries. For instance, Al-Futtaim Sons operated the British brand Marks & Spencer in the Middle East (Burt et al., 2002). Many international retailers intend to sign master franchises for their business activities across the Gulf regions. The Gulf businessmen have excessive money and have political connections, which lead to the spread

of the business through the country (Young, 2001). Maritz et al. (2007) argued that the power of influential people in Saudi Arabia may cause a problem for the franchisor. However, the author claimed in his study that this matter no longer exists and that the Saudi government authorities are fighting this issue to encourage investors to enter the market. Martin (1999) argued that many franchised companies exhibit stable growth in the Saudi market due to their good relations with the members of the royal family or with famous business families who have strong authority in the country. Most of the distributorships and agencies are owned by a few famous Saudi families, such as the Alireza, Bugshan, Jomaih ,Olayan, Juffallis, the Al-Quraishis, and El-Gossaibs, with long experience as retailers (Dunn, 1979; Field, 1984; Kaikati, 1979; Kaitaki, 1976; Stern and El-Ansari, 1982). The Saudi anti-corruption authority have detained eleven princes, ministers and former ministers who were involved in corruption activities and money laundering (Al Arabiya English, 2017). Alon and Alami (2010) claimed that the McDonald's in Morocco is operated by a member of the royal family, which led to the success of the brand. However, the authors stated that there are many franchises business that are doing well and have no relationship with the royal family.

Swartz (1997) described the Middle East, particularly Saudi Arabia, as a 'potential franchising hotspot' owing to a strong competition among its businesses to entice international investors. (See Table 6). The success of franchising in the Saudi Arabian market is ascribed to obtaining a good brand name, and finding an appropriate location (Sadi et al., 2011). Tuncalp (1991) claimed that international franchising in Saudi Arabia begun in the mid-1970s when a Kentucky Fried Chicken restaurant, also known as KFC, was opened in Riyadh city. The franchise models are mostly present in the sector of restaurants, food, beverages and retail (Jehanzeb et al., 2015). Data demonstrates that franchises grew from 45 in 1991 (Tuncalp, 1991) to 200 in 2005 (Alharbi, 2014), and to 305 in 2009 and 335 in 2010, running 1,125 units with 130,000 staff members (Human Resources Development Funds, 2010). Further, the number of franchises increased by 13.7% in 2011 to a total of 381 (Ministry of Commerce and Industry, 2012).



**Table 6. The Distribution of Franchise Businesses in Saudi Arabia (2011)**

| Country  | Number of Franchises |
|--|----------------------|
| United States of America                         | 97                   |
| United Kingdom                                   | 44                   |
| France   | 43                   |
| Italy  | 35                   |
| Lebanon  | 21                   |
| Spain  | 19                   |
| Canada   | 10                   |
| United Arab Emirates                             | 10                   |
| Malaysia   | 9                    |
| Holland  | 8                    |
| Germany  | 7                    |
| Switzerland                                      | 6                    |
| Belgium  | 6                    |
| Egypt  | 6                    |
| Other countries (including domestic franchising) | 60                   |
| Total  | 381                  |

Source. Alharbi (2014)

After the increase of oil production, Saudi Arabia has become a top choice for franchisors for providing innovative models in the food and non-food sectors. The Saudi franchise market is valued at over US \$ 1 billion and is estimated to increase at an annual rate of 10–12%. The rate of paid fees and royalties is projected to be over US \$ 323 million or SAR 1.2 billion yearly. Franchising is a famous and a good strategy to launch consumer-oriented businesses in Saudi Arabia. Franchising covers various business categories, such as fast food, apparel, laundry and dry cleaning services, office temporary services, automotive parts and servicing, restaurants, mail and package services, printing and convenience stores. Recent franchising businesses, such as spas, health clubs, wellness and slimming clinics and trendy fashion labels have captured the attention of the youth citizens (U.S. Commercial Service, 2018). (See Table 7).

Franchising in the food sector topped the list of spending, accounting for more than 17% (about \$ 42 billion), followed by clothing and footwear at 5.66% (more than \$ 13.9 billion). Moreover, there are more than 11 million religious visitors yearly and internet penetration has also supported the continued growth of the retail sector, which led to an increase in the franchising market. The franchising sector will bring more global firms and also encourage more Saudi entrepreneurs to create local concepts, particularly in the food sector. Different factors lead to the positive outlook towards franchising. For instance, the increasing urbanisation and the increasing percentage of well-travelled Saudis (U.S. Commercial Service, 2018). According to the Business Monitor International (BMI) projection, the percentage of Saudi urbanisation by 2050 will increase to 88.7% from 83.1% in 2015. The main urban regions are the capital city, Riyadh, as well as Jeddah. Markets with an advanced urbanisation rate are considered more appealing because of advanced logistics, large consumer contribution and better spending levels. In contrast, consumers in countryside areas are difficult to reach and have lesser spending power. This leads to risky investments, specifically in developing countries (Saudi Arabia Consumer & Retail Report, 2018).

According to MBI, by 2050, Saudi Arabia's population is expected to reach 45.1 mn from 31.6 mn in 2015. This will be an additional of 13.5 mn people over this period, far beyond markets such as Bahrain, which is the smallest country in the Gulf States. The growing population of immigrants also enhances and increases Saudi Arabia's population over this long period. Saudi Arabia is considered a good consumer market, with the highest number of households among its Gulf Cooperation Council (GCC) peers, reaching 5.7 mn by 2022 (Retail & Consumer Report, 2018).

The Saudi franchise market contains restraints that the governmental officials are trying to eradicate. For example, the judicial environment is considered an obstacle to the success of franchising. There is no franchising law that controls and manages the relationship between the principal and agents. Instead, franchising deals with those under the 'Trade Agency law'. For instance, the Saudi brand Al-Baik was the first restaurant to introduce the 'broast' chicken idea in Saudi Arabia. Al Omran (2013) mentioned that the local brand is famous among Saudis who are willing to stand in line for a long time in order to try the broasted chicken, and some Saudis are willing to transport these meals by plane in order to sell them in another city at double the

price. However, the chief executive of the company claimed that there are no franchising laws that protect the local brand owner's ability to penetrate different parts of the country. The company has lobbied for the government to improve the franchising regulations (Al Omran, 2013).

Taqi (2007) stated that there is a need for major improvements in the Saudi legislative franchising framework. Some articles have been attached to the agency law to limit the gaps in the law, which does not have the essential terms and conditions that are required in international franchising contracts (Mikwar and Akkad, 2011). Ali (2008) mentioned that there is a franchise committee in Saudi Arabia that is controlled by the Saudi chambers of commerce management. This franchisee committee represents the role of the franchise associations to a certain degree. There are not enough franchising consultancy services that are capable of helping the domestic Saudi concepts grow and advising them with legal and financial services. Also, sub-franchising is an uncommon concept that has been used in Saudi Arabia because many franchisees come from wealthy families and possess the resources to open outlets without the need to sub-franchise. Saudi Arabia is not the only country that does not have a suitable authorised framework for franchises.

Briggs and Araghi (2009) argued that due to the ambiguous jurisdiction system of the UAE, the franchisor should include clear clauses in the franchise contract in order to implement the arbitration in the franchisor home land problem a rise. In Saudi Arabia, the partners have the right to select an international law pertaining to arrangements that do not need to be registered, such as master franchise agreements and area development agreements. It is considered that arbitration tends to be much more convenient for applying overseas than in a local court, since over 140 countries have agreed to the New York Convention on the acknowledgment and Enforcement of International Arbitral Awards, which include all gulf countries (Young, 2001).

*'Enforcement of an arbitral award requires Court involvement, and Courts will only enforce an award if it does not conflict with Islamic or Shari ah law, public order, morals or, in Saudi Arabia, local law'* (Young, 2001).

Chanut et al. (2013) also contrasted the fundamental differences in the development of franchising between Morocco, Algeria and Tunisia based on three criteria – country risk, existence of modern business structure and law and institutions. The results indicated that Morocco’s institutional environment is the most favourable environment for franchising when compared with other countries because of the trade structure, financial support and establishment of the Moroccan Franchise Association. This demonstrates the importance of developing the institutional infrastructure of the country to attract the international franchisor.

**Table 7. Numerical and Distribution of Franchise Business in Saudi Arabia according to Economic Activities (2009–2011)**

| No. | Economic Activity                         | 2009   |      | 2010   |      | 2011   |      |
|-----|---|--------|------|--------|------|--------|------|
|     |   | Number | %    | Number | %    | Number | %    |
| 1   | Readymade clothes (ladies, men, children) | 91     | 29.8 | 99     | 29.5 | 108    | 28.3 |
| 2   | Shoes, leather products                   | 20     | 6.5  | 23     | 6.9  | 25     | 6.6  |
| 3   | Food, beverages, restaurants              | 76     | 25.0 | 84     | 25.1 | 96     | 25.2 |
| 4   | Coffee shops, pastries, ice cream         | 31     | 10.2 | 34     | 10.1 | 55     | 14.4 |
| 5   | Building materials, electrical equipment  | 14     | 4.6  | 15     | 4.5  | 19     | 5.0  |
| 6   | Education, training, recreation           | 14     | 4.6  | 15     | 4.5  | 17     | 4.5  |
| 7   | Cosmetics, perfumes, optics               | 13     | 4.3  | 14     | 4.2  | 23     | 6.0  |
| 8   | Other sectors                             | 46     | 15.0 | 51     | 15.2 | 38     | 10.0 |
|     | Total                                     | 305    | 100% | 335    | 100% | 381    | 100% |

Source: Alharbi (2014)

### 3.4 Potential Barriers to Franchising in Saudi Arabia

Previous studies mentioned the obstacles that hinder the progress of international franchising in different emerging countries. For example, Alon (2004) identified some of these obstacles, including a lack of experience, a lack of investment by the international franchisor, the political

instability of the host country and the lack of infrastructure in the host country. Sanghavi (1998,p.38) claimed that those barriers are the lack of infrastructure development, the price of importing the materials from the franchisor's homeland is much higher as compared to the market price and the low purchasing power.

Tuncalp (1991) examined the barriers confronted by franchise companies in Saudi Arabia from the franchisor's perspective using the marketing mix (product, price, promotion and location). The author mentioned a couple of issues that still exist today. For example, Saudi franchisees hire managers from neighbouring countries who have no knowledge regarding how to run a franchise business without paying close attention to the operational activities. Also, the author claimed that many franchisors who decided to open in the Kingdom were not conducting proper studies into the acceptability of their products in terms of the social norms of the local customers. For example, Saudi consumers prefer fresh meat over frozen. This is rooted in the culture that most Saudis will purchase live sheep from the outdoor markets and have them butchered and prepared according to their customs. The meat should be slaughtered in compliance with the Sharia law (halal). Meat is considered 'halal' only if a specific religious ritual is followed before and during the slaughter process. For instance, Alon and Alami (2010) stated that one of the reasons behind the failure of Subway in Morocco was the franchisor's lack of market expertise and insufficient pre-market research.

Tuncalp (1991) also claimed that promotion was an issue in the Saudi market unless the franchisors came up with innovative ways to start a business. The author argued that many local Saudi business owners are keen to come up with creative international names to suggest that they are global in order to promote their restaurants and meet the fierce competition using their ability to add local varieties of dishes to the menu .Tuncalp (1991) claimed that numerous franchisees exaggerate the prices of their international brands, which makes them unaffordable for the locals. This could be caused by the high fee of transportation and insurance as well as the customs and import of raw materials from the country of the franchisor. Thus, the franchisors must intervene and control the final price or allow raw materials to be imported from the local market and by the franchisees. They can also stop providing free salt and ketchup to save additional funds.

Alharbi (2014) identified the barriers that prevent franchising from developing, including the lack of legal infrastructure and financial and promotional environments. A study conducted by the Saudi Chamber of Commerce<sup>2</sup> in 2005 found that the lack of an appropriate legislative environment is one of the obstacles that confront both the franchisee and the franchisor. Saudi courts do not always apply contracts professionally. The court system suffers from bureaucracy, lack of transparency and is manipulated by the ruling elite (Mellahi and Wood, 2002; Rice, 2004; Zamberi, 2012). Laws protecting intellectual property rights are being reviewed to conform to those of the World Trade Organisation since the admission of Saudi Arabia in 2005. The protection and implementation of Intellectual Property Rights is weak. (Zamberi, 2012), and international franchisors claimed that the commitment to international treaties and agreements and the effectiveness of the arbitration system by Saudi judicial courts is weak. Maritz et al. (2007) claimed that the protection of intellectual property rights is a challenge for the franchisor due to the absence of the laws related to the system, especially with regard to the protection of uniforms of restaurant employees in Saudi Arabia. Many customers become confused because of the uniformity of clothes, and this may be exploited to bring in customers.

A study conducted by the Akkad<sup>3</sup> (2008) on the Saudi commercial franchise system explores the practical experiences in the field of legal franchises in Saudi Arabia. The study concluded that it is important for the franchisor to register his/her intellectual rights and the most important trademarks prior to the signing to contract. It is also important for the franchisee to determine and investigate the financial status of the franchisor and how many franchisees the franchisor has around the world. It is important for the franchisor to get the franchisee to sign a paper to prevent them from disclosing confidential information before signing the contract, in case the franchisee tries to disclose certain information about their company. This could lead to opportunistic behaviour such as shirking.

Another issue that may impede the success of international franchising is finding the right supply. It is difficult for international franchisors to find reliable suppliers in the Saudi market for providing the franchisee with raw materials (Abughazala, 2006; Maritz et al, 2007). Han

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<sup>2</sup> The study is published in Arabic Language

<sup>3</sup> The study is published in Arabic Language

(2014) argued that the Australian brand Noodle Box had to modify its menu. The company struggled to replace their fresh noodles with dried ones because there were difficulties in finding appropriate Middle East-based suppliers when they entered Saudi Arabia.

The issues of international franchising differ from one sector to another. For example, Yaves and Habib (1987) conducted a study on the car dealers in Saudi Arabia and their relationship with car manufactures. The authors mentioned that there is a lack of training for the salesmen in Saudi Arabia, and the car dealers are not happy with the sales-training support that they receive from the car manufactures. In the hotel sector, Aleidan (2017) claimed that the global hotel franchisors emphasised the importance of establishing tourism-based associations that will help the franchisor access the sector data and make assumptions within the sector in the long run and help them hire Saudi hoteliers with the relevant qualifications and competence. In addition, the establishment of a national tourism centre is essential for the franchisor to have information about the comings and goings of the players within the sector. The hotel franchisors are concerned about the bureaucracy and the long process involved in issuing classification certificates, which lead to high transaction costs. In the retail sector, Hartvigson and Hourani (2009) provide illustrations of issues faced by the IKEA manager in Saudi Arabia. The first IKEA store was set up in 1983 in Saudi Arabia and, today, the country has three IKEA stores. The authors claimed that the business ethics of Saudi Arabia are different from the Western culture. There is difficulty of hiring and finding citizens who speak English. Maritz et al. (2007) found that the majority of franchisors in Saudi Arabia's fast-food restaurants have difficulty finding qualified and trained Saudi workers, which affects the operational quality of the business.

### **3.5 Potential Opportunities Franchising in Saudi Arabia**

#### ***3.5.1 Franchising and Saudi Entrepreneurs***

The term 'entrepreneur' was first used in the sixteenth century in France to define the captains of fortune who hired mercenary soldiers to serve princes and towns. Usage in a business context commenced in the eighteenth century for referring to economic actors who undertook contracts for public works, introduced innovative agricultural techniques or risked personal capital in the

industry (Martinelli, 1996). Schumpeter (1911, p. 89) mentions that an entrepreneur is a leader, who steers the ways of invention into new networks. Entrepreneurs are pioneers and visionaries because their role is to improve or transform the form of production. Shane and Cable (1997) define entrepreneurs as '*individuals who receive their compensation in the form of residual claimancy on the proceeds of a firm and who also have operating control of an organisation*'. In addition, Ahmed et al. (2013, p. 42) define entrepreneurship as '*the discovery of opportunities that had been previously unnoticed*'. Bokhari et al. (2012) argued that entrepreneurship has numerous benefits; it encourages innovation, reduces unemployment rates and meets new consumer demands

Hoy, Stanworth and Purdy (2000) and Shane and Hoy (1996) argued that franchisees are distinct from entrepreneurs; for example, they spend their money in an already established business model that is founded by a franchisor, which reduces their risk as compared to entrepreneurs. Knight (1984) claimed that entrepreneurs are more self-determined as compared to the franchisee. The author investigated the difference between Canadian franchisees and self-reliant entrepreneurs by paying attention to their individual traits, administration abilities, financing and support services. The author mentioned that dissimilarities found in the franchisees are less self-reliant because of their relationship with franchisors. Paswan and Johns (2007) perceived the franchisees as employees instead of business executives running a business. In addition, Sardy and Alon (2007) found that franchisees in the United States differ in their individual traits as compared to entrepreneurs. They tend to have less experience, not confident in their capabilities and ability to succeed in their business.

Franchising is a structural system selected by entrepreneurs in the services domain, where a decentralised system of chains is required in order to attain a competitive advantage (Caves and Murphy, 1976; Lafontaine, 1992; Rubin, 1978). Siggel, Maisonneuve and Fortin (2003) also claim that franchising entrepreneurs are sources of risk-taking and expand their business in developing economies. The authors claimed that fifty-two franchisors from four African countries made an average of 7.5 franchises per year during a period of two to twenty-five years.



It is important to note that a franchise outlet offers two different benefits to the local entrepreneur. First, it offers the benefits of utilising the same trademark via many outlets, unifying the customer's experience across time and location. Second, the franchise saves the franchisees a significant amount of time and develops their advertising skills in their native homeland. A further advantage of utilising the franchise outlets is the technology transfer. The franchisor has launched standard operative procedures or practises in which the franchisor teaches the franchisee. These practises improve performance for the franchisee as compared to local firms that own local restaurants (Knott, 2003). International franchising enables knowledge transfers, technology, and human capital while enhancing the capabilities and skills of the work force (Alon, 2004).

Sanghavi (2001) mentioned that native entrepreneurs in emerging markets benefited from the concepts associated with the administration of a brand name, the brand's well-known reputation and the loyalty to the franchisor company. Alon and Banai (2000) claimed that franchising in Russia educated entrepreneurs to be grateful and imitate the ideas in their local businesses. For example, SME improvement through global franchising in transition economies often occurred in steps following a lifecycle. First, international franchisors penetrate the market through master franchising, joint ventures, or sole venture. These companies establish local franchising through direct or area development franchises. Native entrepreneurs benefit from these new business systems, imitate and alter them according to local taste and become strong rivals by creating their own brands and business formats and forces the international franchisor to leave the market by launching a national sphere of control. By this time, franchisors from these transition economies may find themselves penetrating the international franchisors' marketplace and enhancing the international competition.

Dant et al. (2011) claimed that innovation is an essential element for the franchise companies to compete and survive. For example, in the African context, Siggel, Maisonneuve and Fortin (2003) claimed that franchising allows new technologies to be disseminated, brings new business models to the local market, contributes to the productivity growth and generates external economies. They also noted that domestic franchisors, domestic suppliers and

franchisees account for 25, 20 and 15% of all innovations respectively, whereas foreign franchisors and suppliers account for 20% (Alon, 2004).

In addition, Wu et al. (2009) claim that innovation is extremely important for franchisors to distinguish themselves from rivals and acquire new markets. It is also essential for enticing new franchisees for the business (Watson and Stanworth, 2006; Falbe et al., 1999). Lewin (1999) mentions that research and development and marketing services are the franchisor's main capitals in the context of the growth of innovations. Innovation is a contributing factor for economic development (Szulanski and Jensen, 2008) and business achievement (Rogers, 2004).

According to Oslo Manual (2005, p. 46),

*'The minimum requirement for an innovation is that the product, process, marketing method or organizational method must be new (or significantly improved) to the firm. This includes products, processes and methods that firms are the first to develop and those that have been adopted from other firms or organization'.*

Franchisees play an essential role in innovation development (Bürkle and Posselt, 2008; Cox and Mason, 2007; Sorenson and Sørensen, 2001). Franchisees also play an important role in providing information about the domestic market and successful product or service adaptations (Dyer and Singh, 1998). Knowledge-sharing routines can also be used to share and leverage innovations developed by the franchisees (Darr, Argote, and Epple, 1995) by creating new concepts or altering current ones. They are a source of solving-problem (Kaufmann and Eroglu, 1999). For instance, franchisees in the Jack in the Box fast-food chain have the ability to set a new price strategy, those of Pizza Hut are allowed to create new promotion schemes and those of Hardee's are permitted to create a homemade biscuit for the breakfast menu. At Pizza Hut, franchisees caused the slight alteration of current dishes, such as substituting of the salad-bar patterns and adding new sauces to go with the bread sticks (Bradach, 1998). Franchisees also engage indirectly in the innovation procedure by imposing pressure on the franchisor to add and create new products (Bradach, 1998).

The Saudi government has to diversify its economy by encouraging different types of business activities (Rizvi, 2014). The concept of franchising has been a popular mode of business expansion, especially with the younger generation of entrepreneurs in Saudi Arabia (Sadi et al., 2011). Entrepreneurship is viewed as a catalyst for economic growth and can reduce unemployment rates (Almobaireek and Manolova, 2012). Sadi and Henderson (2011) argued that many Saudi businessmen possess ample capital and a desire to engage in entrepreneurship, but they do not always have the vision to create new business idea and are hesitant to venture out on their own. This leads to opportunities for franchising that has been particularly popular with the younger residents. Mohammad and Ahmad (2012) sought to shed light on the progress of the entrepreneurship culture in Saudi Arabia using the Hofstede model (cultural dimension). The authors claimed that, in order for the Saudi entrepreneurship culture to grow, Saudi Arabia needs to open up and accept changes in order for young Saudi entrepreneurs to prosper and contribute to the economic development of the country. Nunes and Balsa (2013) claimed that Saudi Arabia lags behind countries such as United Arab Emirates, Jordan, and Oman when it comes to supporting entrepreneurship. Saudi entrepreneurs usually have the funds required to run a business. However, they are reluctant to start a business that has a fresh concept, which makes it much easier for Western franchisors to enter the Saudi market (Service, 2005; Ali, 2008).

Entrepreneurship is seen as a means for tackling the lack of job opportunities (Mohammad and Ahmad, 2012; Kayed and Hassan, 2010). Fath (2007) claimed that, by the beginning of the 1980s, international franchises in the restaurant sector helped young Egyptian entrepreneurs open their individual chains that were inspired by Western brands. After a couple of years, a glut of international and Egyptian restaurants were accessible to the customers through many restaurants at affordable prices. The abundance of local and international investment led to economic growth, the demand for franchises business soared and new ideas arose to fulfil the demands of the customers. For example, the idea of home delivery was introduced to the market, which led to the hiring of many Egyptians to work in this position. As customer became regulars, the database became a vital asset. Stimulating sales and saving data also became important, which enhanced the competition.

In their study, Sadi and Al-Fuzai (2010) indicated that franchising has been seen as a successful tool for the business going global, particularly with the younger generation of entrepreneurs in

Saudi Arabia. Most Saudi entrepreneurs choose to get involved with a well-known brand, which helps to grow and maintain their business. There are close to 500 international franchise concepts present in the Saudi market, encompassing areas such as food and beverages, retail, automotive services, health care, education, furniture, hotels, cosmetics, laundry services, apparel, patisseries, juice centres, corn shops and so on. It is also estimated that 20–30 franchise brands are locally conceived, especially in the food and beverage sector, including Herfy, Al-Tazaj, Steak House, Hungry Bunny, Dajen, Dr. Café, Kudu, among others (Ali, 2008).

Indeed, franchising is considered an important business format for the development of the Saudi economy. It allows local small and medium businesses to prosper quickly and helps Saudi entrepreneurs start their business locally and globally. By contrast, Saudi Arabia is a new market with a huge potential for international investors; franchising can be seen as a tool for Saudi Arabia to penetrate international markets (Sadi et al., 2011). For instance, a survey carried out by Bayt.com and YouGov indicated that 67% of Saudi citizens prefer being an entrepreneur. The survey indicated that a large share of both private and public sector workers (62%) think about running their personal business, which leads to opportunities for development across different franchising sectors (U.S. Commercial Service, 2018)

### ***3.5.2 Franchising and the Empowerment of Saudi Women***

The latest figure from the British Franchise Association indicate that 30% of franchise outlets in the United Kingdom are managed by females (Sadler, 2018). Franchising flexibility permits franchises to be managed from home, encouraging the participation of women. One of the potential benefits of franchising in Saudi Arabia lies in the area of female empowerment. Statistics show that unemployment is highest among females. The franchise model gives women with an opportunity for economic empowerment.

There are only a few studies on women entrepreneurs, despite women's influence on the international economy (Ahl, 2006; De Bruin, Brush, and Welter, 2006). Research works on female entrepreneurs constitute less than 10% of all studies in the domain of entrepreneurship (Brush and Cooper, 2012). There is a scarcity of research on entrepreneurial movement of Arab

females as compared to their male counterparts (Dechant and Al-Lamky, 2005; El-Ghannam, 2002; Maysami and Goby, 1999; Abdalla, 1996). The reason for the lack of research that concentrates on women entrepreneurs in the Arab world is that the economic engagement of females relies on social and family control over females and the extent of their freedom as compared to Arab men (Syed, 2011). The unemployment rate of Arab women in the MEANA regions is around 30% (McKinsey and Company, 2011).

Alharbi (2010) mentioned that 80% of unemployed females in Saudi Arabia hold an undergraduate degree. For example, Saudi females are not permitted to have positions in law, accounting and engineering (Nufooz, 2009). Research conducted by LinkedIn claimed that unemployment among women in the Kingdom of Saudi Arabia has slightly decreased from 31.10% in the fourth quarter of 2017 to 30.9% in 2018. Also, the research revealed that 37% of Saudi women believe their employers still need to do more in order to hire them in key roles. The idea that women are not fit or qualified for a job is a myth, believed more than half of women (Damanhour, 2018). Aldagheil (2006) found that Saudi female engagement in the public sector needs to be changed and that there should be a push for women to be hired for high positions, not limiting them to secretarial positions.

Al-Ahmadi (2011) argued that the percentage of Saudi females in the labour market continues to be the lowest in the world, and females are not hired or allowed to be in leadership positions (Al-Rasheed, 2013). The involvement of Saudi women in the labour force is around 14.4%, with the unemployment percentage of female Saudi college graduates being 54%. The Saudi government is now promoting the substitution of expatriate salesmen with Saudi females in its clothing retail stores; however, this has happened without attention being paid to training these young females to be successful in the sector (Alzahrani and Kozar, 2016). The engagement of Saudi females in the labour market is the lowest in the Gulf countries (only 14.4%), while female involvement in the United Arab Emirates labour market is 59%, 42.5% in Kuwait, 36.4% in Qatar and 34.3% in Bahrain (AMEinfo, 2010). The private sector is seen as an opportunity for employing Saudi females, especially in retail. However, female unemployment totals 33%, and the participation rate of women, youths (15%) and senior adults (35%) still fall behind that of mature Saudi males (65%). Alessa (2017) examined the Saudi males' and females' abilities to start and run their

business. The study found that 89.8% of the women participants replied that they had never operated a business as compared to their men counterpart (71.2%). Men were also revealed to be more leading in running their business (28.8%) as compared to women (10.2%). Moreover, men have the tendency to have a greater desire for entrepreneurship and more often wish to leave their occupation in order to open a business.

Abo Ryah (2009) conducted a study at Al Baha University, where there are 1,814 women graduates as compared to 821 men graduates. The author claimed the majority of female students were studying to become Arabic, mathematics, sciences and home economics instructors. However, Alroogy (2009) argued that Saudi universities should focus on majors that equipped students with the ability to be competitive in the workforce upon graduation. In addition, the author mentioned that Saudi female students should be exposed to majors that enhance their ability and skills to work in the private sector. The conclusion was that Saudi universities should develop their programs in order to improve job skills such as accountability, decision-making ability, leadership, providing English language services and technological knowledge.

AlMunajjed (2010) mentioned that 97% of Saudi females work in the finance sector, business services, construction or wholesale/retail trade. Saudi females possess 12% of the companies in Saudi Arabia, of which 16% of the business operates in the manufacture sector (see Table 8). Alturki and Braswell (2010) and Hodges (2017) indicate that female Saudi entrepreneurs are determined, optimistic and tenacious, overcoming the obstacles they confront. The study also mentions that Saudi businesswomen believe that unclear regulations and policies are challenges that negatively impact their accomplishments. For example, the sexism and segregation between the genders is an issue, along with the male guardianship. In a similar study, Zamberi (2011) found that around of 75% of Saudi female entrepreneurs argued that they had some problems when starting their businesses, such as obtaining information, capital support, coping with bureaucratic processes and hiring employees. Nieva (2015) argued that female Saudi social entrepreneurs are different from female Saudi entrepreneurs, and the challenges faced by female Saudi social entrepreneurs include the lack of financing, bureaucratic procedure and gender obstacles.

A study by Welsh et al. (2014) found that female Saudi entrepreneurs have self-assurance in their abilities in terms of coping with people, map storming, creativity, innovation and the ability to manage their business. The author mentioned that females who operate family businesses see themselves as sales generators and innovators as compared to the ones who run non-family business. The author concludes that the issues that prevent Saudi females from running their business smoothly are the difficulties associated with the following: location/high property rent, difficulty in hiring Saudi workers, finding well-trained workers and retaining them, high fees for media/advertising, capital and the male guardianship that prevents them from coping with government organisations and segregation between the genders. Rahatullah (2017) claimed that the determination of Saudi women to start their business comes from their traditional culture. Sadi and Al-Ghazali (2012) stated that self-achievement is the greatest motivating factor for Saudi women to start their business, whereas profits and self-achievement were identified as the most motivating factors for Bahraini women to start their business.

In addition, Afaf et al. (2014) comments *'is a masculine society...strongly influenced by cultural norms and religion'*. The segregation between male and female is compulsory in Saudi society and norms affect all walks of life. The segregation between men and women in the workplace pose a challenge for the government to increase the involvement and contribution to economic development of Saudi women (Mackenzie Global Institute, 2015). According to Business Monitor International (BMI), the restrictions on women's public involvements impede their ability as a demographic to enlarge consumer spending power (Saudi Arabia Food & Drink Report, 2018). According to the research carried out by YouGov, which surveyed 300 Saudi females and 300 recruiters, 52% of recruiters claimed that gender diversity enables higher productivity, and 40% of the recruiters mentioned that diversity leads to a culture of creativity. However, recruiters argued that it is hard to find well-qualified Saudi females (Damanhour, 2018).

However, Leeth (2014) argued that the majority of Saudi females are not ready to accept work that makes them mix or mingle with unrelated males. The social obstacles of Saudi Arabia make it harder for business activities to grow with the integration of women employees. The main concern of married Arab females are their tendency towards their family, which makes it harder

for them to form relationships in their place of work (Hutchings and Michailova, 2014). Ba-Isa (2007) reported one of the major obstacles faced by females engaged in business in Saudi Arabia the lack of support from other females.

Danish and Smith (2012) showed that female Saudi entrepreneurs are able to manage and run more small and medium sized enterprises than they have at any point in the past. The authors interviewed 33 women entrepreneurs in Jeddah city. The authors claimed that the issues faced by Saudi females are associated with their culture and the country's constitution. For example, it might take a Saudi women one month to register her business as compared to females in Bahrain, for whom it takes one hour to do the same (Fakkar, 2007; Afsaruddin, 1999).

Abdullah (2007) investigated the Saudi Arabian laws relating to women citizens. The examination revealed that Saudi females are not allowed to drive, open a business account, obtain a home and invest in real estate. Even the simplest act of reporting a crime to the domestic authorities must be done by a male guardian. Traveling abroad has to be authorised by male guardians (Metcalf, 2008). In, 2017, King Salman of Saudi Arabia released a royal decree that allowed women to drive by June 2018. This decision is a step toward achieving one of the of the government's goals to meet the Vision 2030 strategy – enhancing women's involvement in the Saudi labour force from 22% to 30% (Kane, 2017).

In their research, Al-Mutairi and Fayez (2015) concluded that government regulations must be revised to encourage greater involvement of women in businesses and in the workplace. For instance, hiring specialist woman trainers from outside the country is prohibited because of the restrictions on obtaining business visas for foreign women (Danish and Smith, 2012). The increasing number of female entrepreneurs in Saudi Arabia could lead to socio-economic benefits that will generate a significant amount of wealth. However, Molavi (2006) mentioned that there a slow changes occurring in Saudi Arabia when it comes to business development and female's entrepreneurship. Thompson (2015) claimed that Saudi Arabia has gone through major changes during the past few decades, with females being allowed to be independent, working in the public sector and being hired to be the heads of companies and run their businesses. There is a growing change in the Saudi macro-environment regarding women entrepreneurs.



According to Fakkar (2007), Saudi females are allowed to register their businesses, which was unacceptable until recently. In the mid-2000s, Islamic law gave Saudi females the right to manage their capital; hence, Saudi women are now allowed to do their financial transactions without the intervention of any of their male relatives (husbands, brothers or fathers) (Almunajjed, 2006). Because of the change in regulations and systems, government officials often maintain the use of old laws in country (Alturki and Braswell, 2010). Alotaibi et al. (2017) claimed that the Saudi government has adopted a policy over the last decade to encourage female Saudi involvement in all walks of social, political and economic life, including electing the first woman being elected to the Ministry of Education, involvement in municipal voting and participation in elections for the Chambers of Commerce and Industry. The author insisted that women entrepreneurship development should be expanded to female universities, which will prepare them with the basic skills and abilities to compete in the job market.

**Table 8. The Number of Trade Registries by Women Entrepreneurs in Saudi Arabia**

| Year | Number of trade registries by female entrepreneurs |
|------|--|
| 2007 | 584  |
| 2008 | 825  |
| 2009 | 841  |
| 2010 | 976  |
| 2011 | 1472   |

Source: (Sivakumar and Sarkar, 2012)

### **3.6 The Role of Saudi Culture**

Local culture is difficult to recognise because it is made of many intangible strands (Tyeb, 2003). Francesco and Gold (2005) claimed there is no clear definition of culture. The authors argued that each individual culture has interrelated ideologies. According to Griffin and Pustay (1999),

the main components of culture are religion, language, communication, values and social hierarchy. Culture is known to have a direct influence on a franchising entrepreneurial opportunity (Frederick, 2005). In addition, Harrison et al. (2000) suggested education as one of the main elements that forge a culture. The culture factor has been seen as an important element for firms who are looking to expand globally (Francesco and Gold, 2005). Since culture plays a role in shaping the standard of the service, it is extremely important to address the differences between each country in terms of its norms and values (Zeithaml and Bitner, 2003).

According to Al-Awaji (1971), the main traits of the Saudi Arabian culture lie within the significance of family in the social structure of the clan, the village and the town. The previous studies on culture in Saudi Arabia have indicated that it is homogenous due to the deep influence of Islamic beliefs on the society (Idris, 2007). Islam permeates all walks of life in Saudi Arabia, and there is a committed relationship between Islam and the society (Lundgren, 1998).

According to Dadfar (1984, 1990), the Saudi Arabian culture consists of three different systems: Islam, Tribalism, and Westernisation. Saudi Arabia is seen as the homeland for the entire world's Muslim population because the country has two mosques in Mecca and Medina. Religion shapes the role of gender, ethical principles and the norms of the society. The clanship and tribal system also have a strong influence on Saudi culture. For example, in Saudi society, if you come from the same tribe as the boss who runs the organisation, you might receive a special treatment. Family is extremely important in the Saudi culture, and this has been reinforced by religion (Aldraehim et al., 2013). The trait of cultural, social and economic similarity has led to the forms of homogenous behaviour in the social structure (Baker and Abou-Ismaïl, 1993; Bhuian, 1997a). The culture is impacted by the wisdom of old people through whom the younger generations learn about morals, favourites and customs (Bhuian 1997b; Tunca1p, 1988).

Even with globalisation and the exposure to new technologies in everyday use, consumers in Saudi Arabia maintain their cultural beliefs (DeMooij and Hofstede, 2002). The socio-cultural environment of the Gulf States contains different subcultures among the expatriate residents from different countries, such as Indians, Pakistanis, Thais and Filipinos as well as from other Arab neighbouring countries. This is considered a significant market segmentation that should not to be ignored in terms of price, product etc. (Leonidou, 1991).

Interaction with the Western culture and companies helped enhance the standard of living in the Gulf States through having a good education, better healthcare and improved communication skills (Ali, 1990; Ali and Al-Shakhis, 1986). Currey and Kadash (2002) argued that the Saudi culture is a major obstacle for companies improving and reaching their targets.

*'Maintaining Saudi identity is difficult when contact with the West is needed in order to advance'* (Yamani, 2000).

Fletcher and Brown (2005) mentioned that the franchise entrepreneur's view of the Saudi market depends on the franchisor's cultural experience. For example, the CEO of the franchised American Leak Detection claimed Saudis are not punctual, unlike their American and European customers. For example, if the American customer phone an inspector, the American waits for the inspector at the agreed time. In Saudi Arabia, it can be the other way around; if the inspector arrives at nine, the Saudis will ask him to go out and wait (Martin, 1999). The index of psychic distance grading of countries might prove extremely useful in deciding whether the cultural distance poses a real challenge to franchise businessmen (Barkema, Bell, and Pennings, 1996; Fletcher and Bohn, 1998).

Furthermore, Saudis have the tendency to be more traditional as compared to other Middle Eastern populations (Ali, 2008). Alawi (1986) indicates that older business habits may still exist in Saudi Arabia. The skill of negotiation or bargaining over prices still continues to be relevant. Most shopping in Saudi Arabia is usually intended to be done in the evenings of Thursdays and Fridays<sup>4</sup>. However, the existence of modern retail outlets, such as supermarkets, provide little or no chance to the customer to negotiate. Saudi Arabians tend to be more authoritarian as compared to Kuwaitis. The Kuwaitis tend to be submissive and obey authority and customs. The Kuwaiti citizens tend to be more open-minded to new concepts from the Western civilization than their neighbouring countries from other Gulf States citizens (Ali, 1988).

Hofstede's model (Hofstede, 2001; Hofstede and Hofstede, 2005) has identified five different dimensions for explaining national cultures. These dimensions are heavily reliant on each other. The cultural dimensions are listed as follows:

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<sup>4</sup> A Royal decree was issued, changing the official Saudi weekend to Friday and Saturday.

- Individualism versus collectivism
- Power distance
- Uncertainty avoidance
- Masculinity versus femininity
- Long- or short-term orientation

The model provided scales from 0 to 100, and 76 countries were assessed for each dimension. Each country has a position on each scale relative to other countries. Originally, the country scores were produced in the early 1970s; however, many studies applying Hofstede's model have demonstrated that the country ranking in the data is still valid.

In Saudi Arabia, as reported by Cassell and Blake (2012), the cultural dimension score for individualism is 38, indicating a low individualism culture and suggesting a collectivistic society (see Table 9). Alanazi and Rodrigues (2003) claimed that the Saudi culture is collectivistic and influenced by the religious beliefs of Islam, which controls the social behaviour of the society. The authors claimed that conducting business is influenced by the collective thinking of the Saudis, which illustrates relationships through business dealings (Lundgren, 1998). According to Bhuian et al. (2001), the citizens of Saudi Arabia prefer to be guided by the government and be told what to do in business practices. In Saudi Arabia, honest feedback on performance might be seen as a mean gesture by the company and be considered hostile. In the Arab culture, it is preferable to provide feedback through an intermediary person to stay away from conflict and avoid delivering the incorrect message (Gopalakrishnan, 2002).

**Table 9: Individualism vs. Collectivism - United States vs. Saudi Arabia**

| <b>United States (91)</b>   | <b>Saudi Arabia (38)</b>                                 |
|---|--|
| 'I'   | 'We'   |
| Focus on Progress   | Focus on Tradition                                       |
| Competitive   | Collaborative  |
| Individual Achievement  | Success and Position Ascribed                            |
| 'An Enjoyment of Challenges, and an Expectation of Rewards for Hard Work' | 'Work for Intrinsic Rewards'                             |
| 'High Valuation of People's Time'   | Time is in God's Hands and Delays are the Result of Fate |

Source: (Butler, n.d.; Roberts and Taylor, n.d.; Mind Tools, n.d.). Cited in (Cassel and Blake, 2012)

Saudi Arabia's power distance score is 80, indicating a high power distance in the Saudi society. This indicates that there is a high rate of inequality in the division of wealth and power within the society (see Table 10). Saudi citizens are interested in managerial positions due to the belief that working in low positions is shameful and considered by many to be 'a cause of embarrassment'. This has led to shortage of technical skills and labour staff and the dependency on international expatriates (Idris, 2007). This may justify why approximately 80% of the 7.337 million in the workplace are non-Saudi citizens (CIA, 2011). The open-door strategy among Arabs is extremely restricted. Only a few people are consulted, and the bosses encounter little resistance from their subordinates. In general, joint decisions are not implemented by Arab management (Muna, 1980).

**Table 10: Power Distance - United States vs. Saudi Arabia**

| <b>Saudi Arabia (80)</b>                               | <b>United States (40)</b>                                      |
|--|--|
| Inequality is Acceptable                               | Inequality is Minimised  |
| Rigid/Authoritative Structure<br>Vertical Hierarchies  | Flexible Structures Dominate<br>'Flatter Organisations'        |
| Centralised Decision Making                            | Collective Decision Making                                     |
| Respect for Authority                                  | Respect for Individuality                                      |
| 'Large Gaps in Compensation, Authority<br>and Respect' | Authority and Respect is Minimised                             |
| Fear Boss  | Challenge Boss   |
| Individuals in Power are Privileged                    | 'Supervisors and Employees are Considered Almost<br>as Equals' |

Source :( Butler, n.d.; Itim International, n.d.; Mind Tools, n.d.; Roberts and Taylor, n.d.). Cited in (Cassel and Blake, 2012)

Regarding the uncertainty avoidance criteria, Saudi Arabia scored 68, exhibiting uncertainty avoidance. This indicates that Saudis have a low level of acceptance towards the unknown (see Table 11). Walker et al. (2003) stated that Saudis believe that the ultimate control over any situation is in the hands of Allah. This is the opposite of the American culture, which believes to have control over the environment. For example, a Saudi proverb states, 'There is something good in every delay'. Unpredicted excuses are not tolerated in developed countries

**Table 11: Uncertainty Avoidance – United States vs. Saudi Arabia**

| <b>United States (46)</b>  | <b>Saudi Arabia (68)</b>                                       |
|--|--|
| Risk Inclined  | Risk Averse  |
| ‘Informal business attitude’   | ‘Very formal business conduct with lots of rules and policies’ |
| ‘More concern with long term strategy than what is happening on a daily basis’ | ‘Need and expect structure’                                    |
| Acceptance of Change   | Fear of Change   |
| Value Differences  | “Differences are avoided”                                      |

Source: (Butler, n.d.; Roberts and Taylor, n.d.; Mind Tools, n.d.). Cited in (Cassel and Blake, 2012)

In terms of the masculinity versus femininity dimension, Saudi Arabia’s scored 52, indicating more masculine values in the society (see Table 12). Masculinity includes being self-determined and career-focused, whereas femininity involves tolerance, modesty, unity and carefulness. There is no equal opportunity in career development between men and women because of the traditional believes of the Saudi culture. *‘Men are expected to engage in behaviours that emphasise masculinity, such as being in charge, dominance, and achievement. Women are expected to be nurturing, deferent, and affiliative’* (Cho et al., 2015, p. 409). Metcalfe (2007) argued that women in Saudi Arabia have limited choices when it comes to job opportunities, such as working in jobs like education, social work, and women’s health, as compared to their male counterparts.

**Table 12: Masculinity vs. Femininity - United States vs. Saudi Arabia**

| <b>United States (62)</b>                                     | <b>Saudi Arabia (52)</b>                 |
|---|--|
| Value Opportunity   | Value Good Relationship with Supervisors |
| Less Emphasis on Being Caring/Compassionate                   | Caring/Compassionate                     |
| Favour Large Scale Enterprises                                | Favour Small-Scale Enterprises           |
| Value Recognition/Advancement                                 | Value Cooperation                        |
| Value Sense of Accomplishment from Challenging/Rewarding Work | Value Employment Security                |

Source: (Butler, n.d.; Roberts and Taylor, n.d.). Cited in (Cassel and Blake,2012)

Finally, the long-term orientation score in Saudi Arabia is not mentioned anywhere in previous studies, including Hofstede’s research (Cassell and Blake, 2011). However, Gorrill (2007) mentioned that Saudis are not punctual when it comes to business meetings as compared to Western businessmen due to their obligations to pray five times a day and other religious holidays such as Ramadan and Hajj.

However, as a religious country, international companies who are planning to start a business in the region need to be familiar with the local culture in order to avoid blatant mistakes. Also, they need to keep in mind that there are differences between areas within Saudi Arabia, with Jeddah in the west, Riyadh in the north and Dhahran in the east. For example, when the British retailer Debenhams decided to open in the Middle East, it took the culture gap between west and east into consideration. For example, in Debenhams in Saudi Arabia, a women-only floor has been added in the Riyadh store (Jones, 2003).

Customers in the Middle East like to see the commodities offered in different manners, which means that there is a demand for complete clothing concepts. This is unlike the UK, where women prefer to search for their own clothes. The designer profile is extremely important in the Gulf States, and there is little price resistance. Product and merchandising training has been



essential in stores. In addition, the affluent shoppers in the Gulf States demand high levels of customer service unlike those in the UK, and the company has found that services, such as having a personal shopper, have been very popular. Consequently, more personal shoppers have been trained. A newly married couple from the Gulf prefer buying a complete room, from furniture to decoration, whereas newly married couples in the UK will have a wedding list that contains items for the entire house (Jones, 2003).

Islam is not just a compilation of beliefs and acts of worship. It is also a comprehensive way of life that extends to the follower's social and economic activities (Elamin et al., 2015). The influence of Islam also covers all walks of life in Saudi Arabia, including food, behaviour and language (Rawas et al., 2012). According to Harrison et al. (2000, p. 110), *'Religion is seen as the mirror reflections of the country culture'*. Saudi Arabia is an ultra-conservative country that has Islamic thoughts and religious norms that might contradict the foreign company's values that have different ways of running its business activities (Deresky, 2008). The legislations and economic and social norms in Saudi Arabia and other neighbouring Gulf states are inspired by religion (Furey, 2007).

According to Griffin and Pustay (1999), foreign firms in Saudi Arabia have been influenced by following religious rules. Harrison et al. (2000, p.110) postulated that embracing religious differences and respecting the country's laws can help companies evade high risk. The franchisor should recognise the importance of the religion and norms in gulf countries and adapt to avoid contradictions with consumer beliefs (Furey, 2007).

Many global firms achieved their goal of penetrating the Saudi market and accustomed their standards based on Saudi norms and Islamic thoughts (Deresky, 2008). For example, franchised American Leak Detection had to adapt its water and gas leak detection strategy to meet Saudi local culture and avoid offending Saudi sensibilities regarding access to female areas in their homes. The CEO of the company claimed there was a water leak in one of the Saudi houses that needed to be fixed. However, due to the segregation between men and women, it was difficult for their staff to access the female section. The company found that sending non-Saudi staff usually solved the issue. Daniels et al. (1983) stated that the other side of Saudi life is the strong

privacy of family and home. Welsh et al. (2001) mention that, before entering the Gulf States, international franchisors need to understand that there is a little difference even among each Gulf country. Ali (1990) argued that differences in the culture may lead to different interpretations of the Quran and lead to a discrepancy. Many big brands have assumed that the commonalities that exist in Arab countries (common language and religion) entail that the consumer behaviour is also pan-regional. Success in Dubai is not the same success in Riyadh (Jones, 2003). It is important for the franchise to examine these differences, as it will affect the relationships between the franchisor and franchisee. The franchisor may have to modify their systems, products and human resource policies to reflect these more. Welsh et al. (2001) argued that, in auto retail in Kuwait, the shoplifter was a woman. Thus, in Muslim countries, where salesmen are not allowed to touch women, the international franchisor needs to train their employees regarding how to deal with such situations or hire saleswomen.

Exercising religious principals might affect franchisor standard. It is important for the Saudi local franchisees to adapt their product in accordance with the local demands. One of the most fundamental practices in Islamic religion is praying five times a day (IFA, 2008). Shops and business activities are interrupted by the praying (Griffin and Pustay, 1999). However, the total time of closure of retail shops during the prayer time may amount to three hours every day because of the 30-minute closures five times a day. The prayer time varies from day to day and from city to city. Some of the retailers often see this as an opportunity to refill shelves through their often largely non-Muslim staff. The effect is also reduced by the fact that outlets are open for longer durations. International companies have to adjust their business schedule to adhere to the praying time (Ministry of Commerce and Industry, 2010). Non-Muslim business administration have to recognise the importance of practising the religious duties in Saudi Arabia even if they think it might reduce sales (Francesco and Gold, 2005). Ali (2008) claimed that some places ask all consumers to leave the building and stay outside during the prayer time, whereas other premises permit the consumers to stay inside.

Muslim communities observe the holy month (Ramadan) once every year, during which they fast from sunrise until dawn. The fasting month leads many Saudi citizens to alter their working hours and change eating habits and behaviours. Franchisors could permit their local franchisees

to offer and formulate special menus during the holy month (Ramadan) (Hawkes and Bandyopadhyaya, 2000).

During Ramadan, most Saudis prefer consuming traditional dishes at home. In addition, one of the other obstacles that the franchisees might face is Muslims refraining from consuming products that contain pork or alcoholic ingredients (halal food) (Deresky, 2008). Alrajhi (2008) insists that the supplier who imports goods and products to Saudi Arabia needs to ensure that their materials are in compliance with the Sharia law. Having halal materials is a significant element for Muslim consumers.

Yavas and Glauser (1985) claimed that there are great cultural and religious differences between Western countries and the Gulf States. The authors argued that goods that are accepted in Western countries may be inappropriate in the Gulf regions. Franchise restaurants alter their menu based on the Muslims' religious parameters. The Australian Noodle Box encountered another problem when the company found out, post signing the franchise contract, that one of its products has a small drop of alcohol. Thus, the company decided to get rid of the alcohol drop by, once again, working with the manufacturers (Robb, 2014). The American restaurant Melting Pot had to change its cheese recipe because of the country's alcohol ban. The cheese fondue has a beer base, which is not allowed under the Sharia Law in Saudi Arabia (Butler, 2014). Providing alcoholic drinks is not allowed in Saudi Arabia, and this prohibition applies to similar countries, such as Qatar and Egypt. For example, the American Mexican Melting Pot restaurant had to design a menu of mocktails in order to recover the profits lost by not offering alcoholic drinks on its menu (Kaiser, 2015).

The franchisors need to alter their franchise offerings and operational strategies; for instance, providing halal meat, segregation between genders and avoid proactive advertising (Sadi et al., 2011; Sadi and Alfuzi, 2010; Ali, 2008; Bakar, 2014; US Commercial Service, 2018). Fry (2001) mentioned that Saudi Arabia, despite its wealth and its important role in the Middle East, is an ultra-conservative country. Thus, Western international franchisor need to pay attention to the sensitivity of its culture. It is important to be familiar with Arab culture and understand how the customers behave. The national customs influence the manner in which communication and the

approach towards families and women is carried out. It is also vital for the intentional investor to keep in mind that there are differences between the cities within the Kingdom, with Jeddah in the west, Riyadh in the north and Dhahran in the east.

In Saudi Arabia, women are not allowed to interact with men in the same premises (Deresky, 2008). The religious principals in Saudi Arabia maintain and assert the segregation between men and women in public establishments, such as offices and restaurants (Francesco and Gold, 2005). According to Martin (1999), due to the religious beliefs in Saudi Arabia of separating women in public premises, the design of the restaurant branches should keep separate entrances for families. The courts follow Sharia principles, as derived from the Quran and the Traditions of Prophet Muhammad (peace be upon him) known as the Sunnah. These are the two most essential elements of legislation in Islam (Al-Mutairi and Fayez, 2015).

This segregation occurs in places such as mosques, schools, campuses and sitting and waiting areas in hospitals and restaurants. The franchisor should follow the religious norms, so each restaurant should have two separate dining entrances (IFA, 2008; Ali, 2008). A & W Restaurants had to make alterations to their building design to have 'family areas', in adherence with the local customs of Saudi Arabia (Martin, 1999; US Commercial Service, 2018). Pizza Hut, along with other franchise restaurants, created a family dining section and another one for singles (Deresky, 2008). One of the Starbucks coffee shops in Riyadh placed a sign outside their store stating, *'Please, no entry to ladies. Send your driver to order. Thank you'*. This incident happened after the intervention of the religious police member who forced the manager of the coffee shop to put up the sign after partition wall fell down that separated men from women. This caused outrage worldwide after a Saudi woman posted the sign on twitter in complaint. However, the problem had been resolved (Arab News, 2016). Murphy (2009) argued that gender separation habits in Saudi restaurants are in place in order to prevent male from seeing or sitting near females whom they are not related to by blood or marriage. One section is called the 'singles section', which only serves singles or groups of men. The other section is for families. This is for single females, groups of females, and wedded spouses with or without babies. In addition, females have to work separately from Saudi males and have different exit/entrance doors, which usually cause problems for other foreigners who are not familiar with Saudi culture (Almejmaj et al., 2015).

Saudi Arabia has an ultra-conservative culture that requires different methods for advertising. Douglas and Dubois (1977) mentioned that cultural factors influence advertising in four manners: the choice of advertising concept, the connotation of words and symbols, the way graphic conventions are interpreted and media selection. In Saudi Arabia, religion takes priority over culture regarding its effect on advertising in the country (Luqmani et al., 1989).

Abdul Cader and Wilson (2015) showed that international franchisors who were planning to advertise their products needed to be aware of religious behaviours when delivering advertising contexts and content. The considerations are (1) avoidance of Islamic creedal taboos and displays of immorality. Tuncalp (2001) claimed that when a American franchise company use the word 'hamburger' in its advertisement, it was not acceptable in the Saudi culture because many Saudi customers think the burgers contained ham, even though international franchise companies adapted to the change and used beef burgers instead. Advertisements must be designed in accordance with the Saudi culture and customs (Sohail and Al-Gwaiz, 2013). Johnson (2016) stated that the American restaurant Church's Chicken restaurant operated as Texas Chicken in Saudi Arabia. Ali (2008) mentioned that international franchisors should pay attention to advertising sensitivity that would be seen as only mildly-suggestive in the West, which is not acceptable in Saudi Arabia .(2) Staying away from using musical instruments and taboo content. (3) Women must be dressed modestly and gender-roles must adhere to Islamic teachings. For example, the Saudi hardware retailer Saco has censored an advertisement showing a woman wearing swimsuit. The retailer replaced the woman's picture with an inflatable ball. The photo was edited in accordance with Sharia law, which allowed the company to promote its sale during Ramadan (Akbar, 2017) (see Picture 1 and Picture 2). Finally, the authors indicated that Avoiding misleading marketing, defaming the competition and ambiguous transactions.

Dant and Berger (1996) claimed that cooperative advertising decisions in franchising provide better profits to the franchisor and franchisee than individual advertising decisions. For example, the British retailer Marks & Spencer had opened five lingerie stores in Saudi Arabia and planned to increase the number to 25 stores around the country. The company made some changes in order to open in Saudi Arabia. For example, the company uses headless female mannequins in its stores. In addition, the fashion retailer Zara opened in Riyadh, and the company blurred the

photos of female models on video screens behind the counter to adhere to the country's rules (Jones, 2015). The Swedish retailer IKEA has removed photos of women from the Saudi catalogue, which is against the company corporate culture (Pollak, 2012).

Luqmani et al. (1989) mentioned that Prior approval from religious scholars is important before initiating advertising campaigns involving sensitive concepts. There is no authorised establishment for supervising the adverts in Saudi Arabia. The Ministry of Commerce and Ministry of Information issue rules, which are the proper guidelines for dealing with violations. The unofficial monitoring of advertisements is managed by the Committee for the Promotion of Virtue and Prevention of Vice (the religious police). The religious police (*Mutawa*) was founded by the order of King Abdul-Aziz Al-Saud with the main objective of stopping any immoral behaviours in the society (Al-Abbad, 2009). One of their responsibilities is to screen print and media advertisements for any activity that contradict Islamic teachings (Cook, 2010). Shehadi (1984) claimed that the Saudi Ministry of Commerce stopped adverts that related to sweepstakes after criticism that came from the Council of Ulema (religious scholars) that these conflicted with Islamic teaching against gambling. There were protests about lotteries that were published in the local newspaper by car dealers and supermarkets as a part of their sales campaigns, with slogans such as, 'I won this Mercedes from Juffali'.

Hall (2012) mentioned that Coca-Cola released an advertisement that angered the religious police in Saudi Arabia because the promotion showed a young male and female flirting over a can of Coke. In addition, Coca-Cola issued another advertisement wherein a young male writes his number on can and hands it to a woman. Moreover, Burger King released an advertisement showing two American females and two young Gulf males. One of the American lady shouts 'Y'all must be loaded' and one of the gulf male answers in a broken accent, 'We have oil wells in our backyard OK, and once a week businessmen come to us and we pump the oil by hand'. This advertisement led to a controversy that some of the citizens were not happy to be negatively stereotyped. Lidstone (2003) stated that Mecca cola is one of the successful companies operated by Tunisian entrepreneur that tried to enter the Saudi market as the largest soft drink market in

the Middle East. Saudi Arabia delayed the process because of the use of the holy city's name as a trademark and asked the company to wait for a Fatwa<sup>5</sup> to be issued.

Picture (1) shows the real picture before editing



Source: (Akbar, 2017; Dailymail, 2017)

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<sup>5</sup> Fatwa is a legal pronouncement in Islam, released by a religious law specialist, on a particular issue. Fatwa is released at the request of an individual or a judge to settle a question where “Islamic jurisprudence” is vague.

Picture (2) showing the images after editing



Source: (Akbar, 2017; Dailymail, 2017)

In addition, Pizza Hut caused Saudi rage after they released an advert on twitter making fun of people with impediment. The company used repeated letters to make it look like someone who stutters is reading the text. The people demanded the boycott of the pizza chains around the Kingdom. However, the advert meant to address the International Stuttering Awareness Day and promote the company product (Al-Arabiya English online News Paper, 2017). The German brewery ‘Eichbaum’ released an advertisement that featured the Saudi flag in one of its alcoholic drinks. The company issued the flags of the countries that were a part of the World Cup in Russia on its bottle covers to celebrate the upcoming tournament. The Saudi flag has the statement ‘There is no God but Allah and Mohammad His Prophet’ – a statement of Islamic faith. This advertisement caused anger among Muslims who took action on social media, demanding an apology from the company (Saudi Gazette, 2018). Another example was when McDonald’s depicted the Saudi flag on its take away bags as a part of the 1994 World Cup campaign. Muslims in Saudi Arabia thought that Islam had been humiliated by putting the Islamic slogan on a bag that would be end up in the trash. McDonald’s apologised and withdrew



this bag, otherwise it would have had a negative effect on the franchisee business in Saudi Arabia (Griffin and Pustay, 1999).

Other examples include political boycott when Denmark's biggest newspaper handed out 12 sketches showing Prophet Muhammad as a violent person who encourages acts of terrorism. The Danish newspaper refused to apologise to the Muslim world, claiming this behaviour is an act of freedom. Knight et al. (2009) mentioned that it should be known that, in Muslim countries, offenses made against the Prophet Mohammed are seen not only as blasphemy but also as the severest of all crimes. Four months after the cartoons were released, on Friday, January 20, 2006, religious leaders all over Saudi Arabia urged a boycott of Danish goods as a reaction to the cartoons. Within a few days, an enormous boycott of Danish dairy products began in Saudi Arabia. Danish products, from Lurpak butter to Lego toys, were quickly pulled off the shelves in Saudi Arabia, Egypt, United Arab Emirates, Kuwait, Qatar, Oman, Algeria, Bahrain, Yemen, Tunisia, Jordan and other countries around the Middle East as Muslims waited for an apology for the cartoons (Al-Hyari, 2012). Within the first five days of the boycott early in 2006, the Danish company lost over 60% of its market share in Saudi Arabia (Abosag, 2009). Shortly afterwards, the Danish Arla Foods apologised through a full-page advertisement released in 25 Arab newspapers across the Middle East. The company also supported a number of humanitarian aids in the Arab countries to reduce hostility (Knight et al., 2009). In addition, Justo and Cruz (2009) stated that when Coca-Cola opened its first franchise business in Israel in the 1960s; as a result, Saudi Arabia banned Coca-Cola for more than 25 years.

Periodically, American companies have suffered a backlash after Donald Trump's decision to support Jerusalem as the capital of Israel. Some of Saudi citizens launched a campaign on twitter to boycott American brands such as McDonald's, Starbucks, Burger King and Pizza Hut (Maza, 2017). Previously, Arab students called for the boycotting of Starbucks and other American brands because they believed that these firms supported Israeli interests (Deresky, 2008). Abeidoh (2002) mentioned that the Saudi people boycotted American products and replaced them with Japanese and European goods because of the war between the Iraq and United States. Official US figures showed that US exports to Saudi Arabia dropped by 33%, to \$ 2.8 billion, between September 2001 (the month that suicide bombers, most of them Saudis, hijacked the world trade centre) and March 2002. Abeidoh (2002) and Lewis (2002) mentioned that if Tony

Blair announced a war on Iraq then that would have an impact on British software firms such as Eidos. Anholt (2002) argued that some of the British companies disconnected themselves from UK brands to avoid any boycotting that may occur in the future. The reluctance to purchase the goods of a particular firm or country is the outcome of boycott campaigns that can target either a particular company or all the companies of the target country (Abosag, 2010).

### **3.7 Summary**

This chapter has provided an overview on Saudi Arabia and its economic background. It also discussed the government's desire to diversify its economy away from oil, focusing on the role of international investments in decreasing the unemployment rate and creating job. The chapter also sheds light on the growth of franchising in the Kingdom of Saudi Arabia and the preferred strategies for entering Saudi Arabia such as joint venture and franchising. In addition, the chapter addresses the issues that confront the international franchisor in different sectors of the economy such as restaurant, automobile and retail sector. The chapter highlighted the potential issues that may impede the development of international franchises such as the lack of legal infrastructure, Intellectual property protection and the non-existence of franchise association. The chapter highlights the role of international franchising on the development of entrepreneurial skills of the entrepreneurs globally and on the development Saudi male and female entrepreneurs' focus. Finally, the chapter shed light on the Saudi culture and religion and how these two components may impede the success of international franchise such as the adapting to the local taste and religious norms of the country such as gender segregation, closing during prayer time and dealing with Ramadan. The next chapter will discuss the methodologies that used in this study

## Chapter 4: Methodology

### 4.1 Introduction

*“Methodology is a systematic approach or framework that is concerned with the research process from the theoretical foundation to the collection and analysis of data”* (Collis and Hussey, 2009, p. 73).

Lewis and Thornhill (2003) defined research as *“something that people undertake in order to find out things in a systematic way, thereby increasing their knowledge”* (p. 3). Saunders et al. (2009) stated that a meaningful research project should combine two main elements – the desire to add to knowledge and a robust and systematic research plan. Research has different phases that may vary depending on the discipline concerned, but any researcher is likely to go through the process of reviewing the literature, collecting and analysing data using appropriate methods and then presenting the results (Saunders et al., 2009).

Gray (2004) identifies three different types of study: exploratory, explanatory and descriptive. However, Robson (2002) argued that that the aim of the study may change over time. The purpose of the exploratory study is to explore – *“what is happening; to seek new insights; to ask questions and to assess the phenomena in a new light”* (Robson, 2002, p. 59). On the other hand, the purpose of an explanatory study is to determine the correlation between variables (Saunders et al., 2007). A descriptive study intends to provide information about the phenomenon as it already occurs (Hedrick et al., 1993). As this study pertains to explore the appropriate franchise models in emerging market such as Saudi Arabia and as there is a little known about this contemporary phenomenon in Saudi Arabia, the researcher intends to explore the relationship between the international franchises and different dimensions of the Saudi context.

This chapter explains the approach adopted in the study. The aim and objectives of the study have been discussed. In addition, the chapter will explain the methodology used by the researcher to collect empirical data. Moreover, the research philosophy, research paradigm and research strategy will be discussed in detail and justified. The researcher intends to employ two

methods to obtain data through a case study approach – semi-structured interviews and document evidence. After reviewing the literature, the researcher recognised that there was a lack of empirical studies on the franchising field in Saudi Arabia (Sadi and Al-Fuzai, 2010; Tuncalp, 1991; Alharbi, 2014; Abughazala, 2006; Sadi et al., 2011; Sadi and Henderson, 2011) and even fewer studies that used a qualitative approach with a case study strategy.

## **4.2 The Research Question**

### **Aims of the Research:**

This study aims to explore the appropriateness of different franchise models in the context of emerging market such as Saudi Arabia

### **Objectives of the Study:**

- To explore the role of international franchising for local SMEs, entrepreneurial development, technology transfer and employment in the restaurant sector of Saudi Arabia
- To determine the obstacles, if any, that may impede the operations of international franchising in Saudi Arabia, such as culture, religion and regulations.
- To explore the applicability of agency theory within the context of Saudi Arabia.

## **4.3 Research Philosophy**

According to Saunders et al. (2007), a research philosophy is “*related to the development of knowledge and the nature of the knowledge, the research philosophy contains important assumptions about the ways in which the researcher views the world*”. There are two main views regarding the nature of knowledge – the positivist paradigm and the interpretivist paradigm. Collis and Hussey (2009) suggest that positivism is a paradigm that originated in the natural sciences and rests on the assumption that social reality is singular and objective, unaffected by the act of investigation. This type of research uses a deductive process with an aim to provide

explanatory theories with which to understand social phenomena. On the other hand, interpretivism has the underlying assumption that social reality exists in the mind and is subjective. Therefore, social reality is affected by the act of investigating it. This type of research involves an inductive process with a view to provide an interpretive understanding of social phenomena within a particular context (Collis and Hussey, 2009). The researchers also suggest that the main purpose is to treat people as separate from their social contexts and hold that they cannot be understood without examining their perceptions of their activities.

According to Guba and Lincoln (1994), there are three different components of a research philosophy – ontology, epistemology and methodology. Ontology is a philosophical assumption about the nature of reality and the specification of a conceptualisation (Collis and Hussey, 2009, p. 337). Epistemology is “*a philosophical assumption about what constitutes valid knowledge in the context of the relationship of the researcher to that being researched*” (p. 334).

Crotty (1998: p 3) defines epistemology as “*The theory of knowledge rooted in the theoretical perception and thereby in the methodology. It is the approach of understanding and justifying how we know what we know*”.

Methodology is the technique used by the researcher to gain knowledge and a better understanding of the phenomena. Methodology is “*The technique, plan of action process or design lying behind the desire and following techniques and connecting the choice and use of methods to the preferred results*” (Crotty, 1998, p. 3). (See Table 13)

In addition, Guba and Lincoln (1994) synthesise scientific paradigms into four categories – (1) positivism, (2) realism, (3) critical theory and (4) constructivism – highlighting the differences in ontology, epistemology and methodology between each. Hunt (1991) mentions that constructionism provides a methodology for investigating the beliefs of individual respondents rather than investigating an external reality, such as the tangible and comprehensible economic and technological dimensions of management

**Table 13. The Research Paradigms**

| <b>Elements</b> | <b>Positivism</b>  | <b>Critical theory</b>  | <b>Constructivism</b>  | <b>Realism</b>  |
|-----------------|--|---|--|---|
| Ontology        | Reality is real and understandable                       | “Virtual” reality is shaped by social, economic, ethical, political, cultural and gender values, crystallised over time | Multiple local and specific “constructed” realities                          | Reality is “real” but only imperfectly and probabilistically apprehensible  |
| Epistemology    | Objectivist findings – true                              | Subjectivist, value-mediated findings   | Subjectivist, created findings   | Modified objectivist findings – probably true   |
| Methodologies   | Verification of hypotheses, chiefly quantitative methods | A “transformative intellectual” who changes the social world within which the participants live                         | Researcher is a “passionate participant” within the world being investigated | Investigation of research is done by qualitative and some quantitative methods, such as structural equation modelling |

Source: Guba and Lincoln (1994) from (Ben Mansur, 2013)

Many empirical studies of franchising take a positivist philosophy where there is more interest on pure reality (Alexander, 1990, Vida, 2000). A positivist philosophy seeks to justify the objective reality of the hypothesis tested. It prevents problems that could arise from external factors that influence the hypothesis (Bryman and Bell, 2007). According to Elango and Fried (1997), franchising studies are focused on the reality, where knowledge might be influenced by gaining and analysing the external environment.

In contrast, realism allows the researcher to explore reality and consider its distortion from the human and external environment. A qualitative approach is often utilized by a realist researcher to gain a deeper understanding of the process, which allows the researcher to potentially link variables (Fisher, 2010). The study's objectives could be accomplished by utilizing qualitative methods to provide the additional opportunity to understand the specific situation in detail (Elango and Fried, 1997). International franchising research depends on qualitative methods for explaining the situation in detail (Sparks, 1995). A realist approach allows the researcher to comprehend and recognise "*universal laws of cause and effect*" in the social world (Daymon and Holloway, 2011, p. 7). In this research, a realist philosophy adopted due to the nature of the research objectives. Moreover, the inductive method will be used in this research due to the gap in the information about franchising and the favourite franchise models that are used in emerging markets such as Saudi Arabia. Qualitative methods will be adopted within this inductive approach in order to obtain in depth information and analyse it to build a theory based on the new findings.

Crotty (1998) rejects the objectivist view of human knowledge and holds that there is no objective truth waiting to be discovered. Truth, or meaning, comes into existence in and out of people's engagement with the realities in the world (Crotty, 1998). Interpretive researchers are less likely to be narrow and restrictive and usually use more flexible methods (usually qualitative) within an inductive methodological approach (Veal, 1997). In contrast to the deductive methodological approach, an inductive approach tends to derive theories or models from the data gained from the field, rather than trying to test previously prepared hypotheses. In this respect, the induction process begins with a definition of the researched phenomenon (Veal, 1997). Therefore, the researcher engaged with the interviewees to understand their perceptions, interpretations, and how they construct the reality of the economic benefits of international franchising through their experiences working in the restaurant sector as well as their feelings and interactions with these new phenomena. In addition, Denzin and Lincoln (1998) asserted that qualitative research emphasizes the process of discovering how social meaning is constructed and stresses upon the relationship between the investigator and the topic being studied). (See Table 14)

**Table 14. Differences between Interpretivism and Positivism**

| <b>Positivism Paradigm</b>          | <b>Interpretivism Paradigm</b>     |
|-------------------------------------|------------------------------------|
| Tends to produce quantitative data  | Tends to produce qualitative data  |
| Uses large samples                  | Uses small samples                 |
| Concerned with hypothesis testing   | Concerned with generating theories |
| Data is highly specific and precise | Data is rich and subjective        |

Source: Collis and Hussey (2009, p. 62), adapted from (Ben Mansur, 2013)

#### **4.3.1 Qualitative versus Quantitative Research Methodologies**

According to Bryman (1988), the decision to choose a specific methodology should be based on its suitability to answer the research questions. Berg (2001) distinguished qualitative and quantitative research, arguing that qualitative research referred to the meanings, concepts, definitions, characteristics, metaphors, symbols and descriptions of things, while quantitative research referred to the measures and counts of things. Qualitative and quantitative research approaches differ in some major areas, including their analytical objectives, the types of questions posed, the types of data collection methods used, the types of data produced and the degree of flexibility in study design (Mack et al., 2005). Snape and Spencer (2003) indicated that qualitative research is a naturalistic/interpretative approach concerned with understanding the meaning people give to the phenomena within their social settings. Moreover, Strauss and Corbin (1998) suggest that qualitative methods can be used to understand any phenomenon about which little is known, gain new perspectives on concepts about which much is already known or gain more in-depth information that may be difficult to convey quantitatively. As a result, researchers adopt a qualitative approach to examine issues related to individuals or phenomena (Strauss and Corbin, 1998).



The researcher will adopt a qualitative approach in order to collect data for the current study. According to Young et al. (2000), there is a need for more qualitative studies in franchising research. He claimed that over the period 1986–1999, the percentage of qualitative research in franchising was 7.7%. The lack of diverse methodologies in the literature on franchising (Lashley and Morrison, 2000) and too much reliance on quantitative methodology (Gauzente, 2002) have also been criticised. For the purpose of this explorative study, the qualitative inquiry study approach is employed. Jack and Anderson (2002) mentioned that the power of the qualitative method lies in its ability to deliver situated perceptions, dig into details and rich explanations.

Moreover, previous studies on franchising generally adopted quantitative approaches in Saudi Arabia. The researcher adopted a qualitative approach to explore the appropriateness of different franchise models in the context of emerging market such as Saudi Arabia and the issues related to the phenomena, such as barriers that impede the success of franchising in the restaurant sector. The qualitative approach helps the researcher dig deeper and better understand the phenomena. It is an approach that allows answering the research questions by providing rich data and meanings regarding how franchising contributes to economic growth in Saudi Arabia. Franchising is a relatively new phenomenon in Saudi Arabia, and this study is an exploratory study to demonstrate the benefits of international franchise to the Saudi economy in terms SMEs development, entrepreneurial skills, technology transfer and providing jobs in the restaurant sector. In addition, the study is conducted in a particular geographical and cultural context – that of Saudi Arabia. As Gray (2004) mentioned, qualitative research is distinguished as a highly contextual approach, where data is gathered over long periods and in natural real-life settings.

#### **4.4 Research Approach and Research Strategy**

Research approach is essential as it provides a framework for establishing and interpreting the research (Lincoln and Guba, 1985). There are two primary research approaches – deductive and inductive. Through a deductive approach, the researcher develops a theory and hypothesis and designs a research strategy to test the theory (Saunders et al., 2007). On the other hand, deductive

research is the approach wherein theory is tested through empirical observation (Collis and Hussey, 2008). Inductive research is defined as an approach in which a theory is “*developed from the observation of empirical reality; thus general inferences are induced from particular instances*” (Collis and Hussey, 2008). The inductive approach generally requires an in-depth inquiry into a social or human problem from multiple perspectives. It begins with an empirical investigation in order to develop a corresponding theory (Yin, 2009). Moreover, in the inductive approach, the researcher does not begin with a theory but aims to conclude with one, developed systematically using the data collected (Hammersley, 1992).

One of the most important differences between the deductive and inductive approaches is how the existing literature and theories are used to guide the research carried out within these approaches. As the deductive approach is designed to test a theory, the literature is used to identify questions, themes and inter-relationships before data is collected (Creswell, 1998). The inductive approach, however, constructs theory as the research progresses; themes are identified throughout the research process and the literature is used to explore a range of topics and generate background knowledge concerning the topic in question (Creswell, 1998).

This study will use an inductive approach as its main guide for conducting the empirical investigation. The inductive approach will enable the researcher to outline the nature of the relationship between theory and research (Gilbert, 2003). According to Ghauri and Gronhaug (2005), “*qualitative methods are more suitable when the objectives of the study demand in-depth insight into a phenomenon*”. Saunders et al. (2007) noted that the inductive approach provides an opportunity for further explanation of what is going on.

After identifying the research problem or question, the selection of a research strategy is one of the most important decisions made by the researcher. It dictates the major direction, narrows the range of research tactics and dictates much of the detail that the actual work will follow (Remenyi et al., 1998). Easterby-Smith et al. (2004) and Gray (2004) suggested that qualitative research is often associated with inductive research designs, in which a range of methods are used to collect data to explore the problem from different perspectives. The researcher can use various strategies to collect information for study. According to Myers (2009), the qualitative approach comprises case studies, ethnographic studies and action research. In addition, Saunders et al. (2007) point out that the qualitative approach may include experiments, surveys, case

studies, ethnography and action research, cross-sectional and longitudinal studies. There are many research strategies used in social science research (Velde et al., 2004), including experiments, surveys, histories, analysis of archival materials and case studies.

Yin (2008) provides three criteria that can be used to select the appropriate strategy for a certain research:

1. The type of research question posed
2. The extent of control an investigator has over actual behavioural events
3. The degree of focus on contemporary as opposed to historical events

The researcher will adopt the case study as a strategy to collect data. According to Yin (2008), the case study is a research strategy that involves empirical investigation of a particular contemporary phenomenon in its real-life context, using multiple sources of evidence. Building theory from case studies is a research strategy that allows using one or multiple cases to arrive at theoretical constructs based on empirical evidence (Eisenhardt, 1989b). Yin (1994) noted that case studies are rich, empirical explanations of specific situations concerning a phenomenon that rely on multiple data sources. A characteristic of the case study is the concentration on a particular site. Yin (1994) claimed that the use of case studies gives the researcher the opportunity to use multiple sources to collect data, which will help the researcher triangulate and enhance the credibility of the data. Yin (1994) also argued that using a case study limited the researcher's ability to generalise the results.

Since the case occurs in a specific social and physical setting, the phenomenon and the context cannot be isolated from each other (Robson, 2002). The case study has an established place in international business (IB) research. A recent review of articles published in four core IB journals over a ten-year period found case studies to be the most popular qualitative research strategy (Piekkari, Welch, and Paavilainen, 2009). Furthermore, Lubbe (2003) and Robson (2002) suggest that a case study approach is suitable for an empirical enquiry into a contemporary phenomenon. The researcher selected a case study strategy in order to explore the appropriateness of different franchise models in the context of emerging market such as Saudi Arabia in-depth, focusing on the restaurant sector. In addition, there is a lack of empirical studies

that used the case study strategy as a qualitative method in the franchising field. Furthermore, a case study is a useful strategy to implement, especially if the target country has a different culture, such as Saudi Arabia. The researcher can also use multiple methods for data collection, such as interviews and document evidence (Yin, 2003).

Perry (1998) pointed out that there are no precise guidelines for the number of cases to be included in a study, although Voss et al. (2002) stated that the fewer the cases, the greater is the opportunity for in-depth observation. Voss et al. (2002) further argued that, although a single case study offers a greater depth of understanding, it places limitations on the generalizability of the conclusions drawn. It could additionally lead to bias, such as a possible miscalculation of the representativeness of a single event and the exaggeration of easily available data. Yin (2009) argues that multiple case studies may be preferable to a single case study and that, when the researcher opts to use multiple cases, it can enhance external and internal validity. In addition, multiple cases enable comparisons that clarify whether an emergent finding is simply idiosyncratic to a single case or is consistently replicated by several cases (Eisenhardt, 1991).

Perry (1998) claimed that adopting multiple cases is common in postgraduate research, as cross-case analysis enables the researcher to better understand the phenomena. The researcher used a single case study which gave the researcher a better and clearer understanding of the phenomena and limited generalisation through focusing on restaurant sector. The interviewees were selected from thirty-one different companies operating in the restaurant sector. The interviews took place in Riyadh, Dammam (Alkobar city) and Jeddah, where the majority of the local franchise companies are located. Denscombe (2007, p. 41) states *“It is pragmatic for the investigator to choose the case which involves the least travel, the least expense and the least difficulty when it comes to gaining access”*.

#### **4.4.1 Data Collection Methods**

There are several methods that can be adopted to collect research data. With quantitative methods, the researcher attempts to measure variables or count occurrences of a phenomenon. In contrast, qualitative methods allow the researcher to emphasise the meanings and experiences related to the phenomena (Collis and Hussey, 2008). Primary data refers to the collection of data

though interviews, direct observation, participant observation, focus groups and questionnaires (Saunders et al., 2007; Collis and Hussey, 2008).

Yin (2003) noted six potential sources of data that can be used in case studies:

1. Interviews: One of the most important sources of information in case studies; should be conducted in person
2. Documents: These provide specific details that can support verbal accounts and could take the form of letters, memoranda, agendas, administrative documents, newspaper articles or any document related to the investigation.
3. Archival records: These include service records, organisational records, lists of names, staff and payroll records, historical correspondence and other such records.
4. Direct observation: This is a means of collecting reliable evidence and could include, for example, field visits.
5. Participant observation: This approach suffers from major problems due to the potential for bias and therefore needs to be used with considerable care.
6. Physical artefacts: These include technological devices, tools, instruments or other physical evidence that may be collected during the study as part of a field visit.

According to Yin (2003), a combination of multiple sources of evidence can help clarify the real meaning of the phenomenon being observed, which might lead to complementary data collection or the triangulation of data.

#### **4.4.2 Interviews**

Hussey and Hussey (1997) define interviews as a “*method of collecting data in which selected participants are asked questions in order to find out what they do, think or feel*”. Interviewing is a research method that involves the interaction between a researcher and an interviewee, with the intention of gaining information from the latter (Robson, 2002). There are various forms of

interview design that can be developed to obtain extensive, rich data utilizing a qualitative investigational perspective (Creswell, 2007). There are three formats for interview design that will be explored, summarized by Gall, Gall, and Borg (2003): (a) informal conversational interview, (b) general interview guide approach and (c) standardized open-ended interview. Sekaran (2003) additionally points out that interviews are conducted to obtain information on the issue of interest. In order to be able to provide information, the interviewees have to be knowledgeable in the areas of specific interest to the researcher. The interviewer should ask each interviewee the same questions in precisely the same tone of voice. The interviewer should have the opportunity to identify non-verbal clues, for example the inflection of the voice, facial expressions or the clothes worn by the interviewee. These factors can subsequently be used in developing secondary questions (Easterby-Smith et al., 2004, p. 86).

The primary reason for conducting qualitative interviews is to understand how individuals construct the reality of their situation from the complex personal framework of beliefs and values that they have developed over their lifetime (Easterby-Smith et al., 2004, p. 86). Anderson (2009) explains that the key issue is to determine the type of interview most suitable for collecting the information required. Anderson (2009) adds that each individual type of interview has implications on the approach taken by the interviewer and will affect the questioning as well as the recording of the data and subsequently, the analysis.

The semi-structured interview with open ended questions was selected by the researcher. Jankowicz (2005) suggests that semi-structured interviews are a powerful data collection technique when used within the context of a case study research strategy. The researcher used semi-structured interviews to explore the interviewees' views, thoughts, beliefs and experiences on the role of franchising as an organisational form in the development of SMEs. The use of open-ended questions allows the flow of information to be gained and permits the researcher to probe further. Tuncalp (1988) claimed that Saudis are not in favour of the survey method in general and filling out questionnaires in particular. They are resistant to taking part in lengthy questionnaire research. The semi-structured interview will be used as the data collection method for this research as its flexibility assists the researcher to modify the questions and possibility save time.

In addition, semi-structured interviews give the researcher the opportunity to probe for more detailed information by asking the respondent to clarify the initial answer. This is significant for those who adopt a phenomenological approach because a primary concern is understanding the meanings that the respondents ascribe to various phenomena (Saunders et al., 2007). However, the interview is also influenced by the level of awareness and emotional state of the interviewee, and a possible distortion to data may occur as a result of the interviewee being anxious or annoyed during the interview (Patton, 2002). May (1997) stated *“To avoid having biased data, the researcher should maintain his own knowledge and let the interviewee flow”*. The researcher chose to carry out in-depth interviews with companies that operate within the restaurant sector to gather empirical evidence on the role of franchising as an organisational form in the development of SMEs. The researcher met key decision makers, such as the executive officers, operations managers directors and general managers, and listened to their views, beliefs, knowledge and experiences. The interviews were conducted with each individual with open-ended questions to gain a clear perceptive of the role of international franchise in the development of SMEs, Job creation and technology transfer in the restaurant sector. The in-depth face-to-face interview is a one of the most qualitative methods by which to discover the complexity and difficulty of different points of view in different companies or countries (Katsikeas et al., 1997; Gummesson, 2002).

The interview questions were designed in relation to the literature (theatrical framework) on franchising in general, including the few studies related to the Saudi context. The interview questions focused on three main concepts: (i) the role of franchising in the development of SMES and entrepreneurial development, (ii) job creation and transfer of technology, (iii) the issues that impede the international franchising, such as culture, religion and internal regulation and (iv) the issues that impede the progress of the relationship between the franchisee and the franchisors through employing the agency theory to Saudi context , such as royalty fees, controlling ,monitoring and asymmetry of information.

The interview questions were first written in English, then translated to Arabic. The cross-linguistic comparability of the English and Arabic versions were checked by a third person who is bilingual in English and Arabic. The researcher also checked with other Arab students who are

bilingual and study at the University to deliver the right message to the target interviewees. The researcher gained access to thirty-one Saudi companies, some of which operated multiple international brands in the restaurant sector and fashion retail. These companies in total managed seventy-five international brands with different brand nationalities, such as American, British, New Zealander, French, Turkish, South African, Thai, Lebanese, Spanish, German, Jordanian, Emirati and Australian, and different categories (fast food, casual dining, and fine restaurants, coffee and bakery). The researcher then carried out face-to-face interviews with 45 individuals with different nationalities and managed to carry out multiple interviews within some organizations (see Table 15). The interviews took place in three major cities – Saudi Arabia: Riyadh, Jeddah and Al-Khobar. These cities are where the majority of business is located and fast-growth companies are located in these cities (US-Arab Tradeline, 2010)

Twenty-six interviews were conducted between July 2016 and November 2016, while the rest were conducted between December 2016 and February 2017. At the beginning of each interview, the researcher explained the purpose of the study and promised that the data would be presented anonymously. The researcher managed to conduct face to face interview with CEOs, directors and general managers of the companies. The interviews lasted between 50 minutes to 2 hours and some interviews lasted for four hours. The researcher conducted some interviews twice with individuals to gain more depth. The researcher observed that some interviews were conducted with the attendance of someone who was in a higher position.

All interviews were recorded with the permission of each participant, except for two interviews where the researcher took notes. After these two interviews, the researcher immediately remembered what had been said during the interview and wrote it down. Some of the interviews were conducted in English, either based on the interviewees' desire (two Arabic native speakers asked the researcher to conduct the interview in English) or because the native language of the interviewee was English. The researcher thanked all participants and promised to provide them with a summary report of the findings and recommendations of the study. In addition, after finishing the interview, the researcher either emailed the participants or used WhatsApp to thank them again, assuring them about the confidentiality. The researcher used the university email as a means of assuring the interviewees that the researcher was conducting the study for academic



purposes; the researcher also carried his university ID with him to assure the participants of the same.

**Table 15. The Interviewee’s Position and the Category of the Restaurant.**

| <b>Company</b>   | <b>Interviewee’s position</b>  | <b>Restaurant Type</b>           |
|------------------|--|----------------------------------|
| C <sup>6</sup> 1 | -Chief Executive Officer<br>(R <sup>7</sup> 1)                           | Casual Dining                    |
| C2               | - Master franchisee<br>(R2)  | Casual Dining                    |
| C3               | -Operation Manger (R3)   | Coffee shop and<br>Bakery        |
| C4               | -Human Resource Specialist (R4a)<br>-Marketing Manager (R4b)             | Fast Food                        |
| C5               | -Administrative Manager (R5)   | Fast Food and<br>Casual Dining   |
| C6               | -Director of Country Operations (R6)                                     | Fast Food and Casual<br>dining   |
| C7               | -Development & Pre-opening Manager<br>(R7a)<br>-Operations Manager (R7b) | Milkshake Bar and<br>coffee shop |

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<sup>6</sup> Refers to a company

<sup>7</sup> Refers to a respondent

|      |  |   |
|------|--|---|
| C8   | -Operations Director (R8)  | Casual Dining                                     |
| C9   | -Human Recourse Director (R9a)<br>-Chief Business Development Officer (R9b)<br>-Brand Development Director (R9c) | Casual Dining and<br>Fast food and coffee<br>shop |
| C10  | -General Manger (R10a)<br>-Marketing Manger (R10b)   | Fast Food   |
| C11  | Chief Executive officer (R11)  | Fast Food   |
| C12  | -Public Relations Officer (R12)  | Casual Dining and<br>coffee shop                  |
| C13  | -General Manager (R13b)<br>- Financial Manager (R13a)  | Casual Dining                                     |
| C14  | -Franchise Expert (R14)  | Expert  |
| C 15 | -Brand Operations Manager (R15)  | Casual dining                                     |
| C16  | -Regional Marketing Manager (R16)  | Fast food and coffee<br>shop                      |
| C17  | -Operations Manager  | Fast food   |
| C18  | -Deputy Chief executive (R18a)<br>-Logistic director (R18b)  | Fine Dining                                       |
| C19  | -General Manager (R19)   | Fast food   |

|     |  |   |
|-----|--|---|
| C20 | -Operations Manager (R20)  | Casual Dining                               |
| C21 | -Business Development Manager (R21a)<br>-Senior Talent officer (R21b)<br>- Financial Manager (R21c)<br>- Operations Manager (R21d)<br>-Strategic HR Manager (R21f) | Fast food                                   |
| C22 | -Owner (R22a)<br>-General Manager (R22b)   | Casual Dining                               |
| C23 | -Operations Manager (R23)  | Fast food                                   |
| C24 | -Franchisee & Development Manager (R24)  | Fast food                                   |
| C25 | -Human Resource Director (R25)   | Casual dining and fast food and coffee shop |
| C26 | -Director, Franchises Relations & Contracts (R26)  | Fast food                                   |
| C27 | -Operations Manager (R27)  | Fast food                                   |
| C28 | -General Manager (R28)   | Casual Dining                               |

|     |  |           |
|-----|--|-----------|
| C29 | -Operations Manager (R29)  | Fast food |
| C30 | - Executive Manager (R30a)<br>-Business Development Manager (R30b) | Fast food |
| C31 | -General Manager (R31a)<br>-Chief Executive Officer (R31b)         | Fast food |

#### 4.4.3 Documentary Evidence

A document provides information about the researched phenomenon and exists independent of the researcher's actions. It is used for specific purposes, other than those of the research, but can be employed by the researcher for cognitive purposes, e.g. letters, newspapers, diaries and websites (Corbetta, 2003). Yin (2003, p. 87) determined that *"For case studies, the main purpose of documents is to ensure and provide supporting evidence from other sources"*.

Corbetta (2003) mentioned the benefits of using documents in investigating phenomena as follows: (a) It helps the researcher avoid the distortion of the results, (b) it guides the researcher to look up the company history and (c) it is not costly and time consuming, as long as the data has already been exposed (Denscombe, 1998). Documents enabled the researcher to triangulate data (Mcmilan, 2015). However, these documents may have drawbacks and may not be reliable sources for gathering data (Patton, 2002). As Miles, Huberman and Saldana (2014) mention, the use of documentary evidence may include biased views and the researcher must thus recognize that they may not precisely represent the outcomes.

Regarding the documents, the researcher used existing materials from internet websites and received a few documents from the case companies; most documents were materials from the company websites. The researcher collected documents about the companies through the internet, such as articles and newsletters, but the majority of it proved meaningless for this research. The majority of companies were not interested in sharing or did not have any written

materials. Atkinson (2007) notes this is compounded by “*the fetish for secrecy that permeates business and society in Saudi Arabia*”. It is difficult to collect secondary data as the majority of national firms in Saudi Arabia do not have marketing or research and development departments (Tuncalp, 1988). Secondary data was not accessible for public use, particularly data controlled by the government and other organizations in the Gulf States (Leonidou and Rosside, 1995).

#### **4.4.4 Sample Frame and Case Study Selection.**

This study used purposive techniques to select Saudi companies. This allowed the researcher to choose companies that would answer the study questions. A purposive sampling approach was used to identify a sample from different Saudi companies operating in the restaurant sector. In purposive sampling, the researcher has to use personal judgement to select companies that will best meet the research questions and objectives (Saunders et al., 2007). In addition, the study is exploratory and uses qualitative methods, so it has appropriate target participants who are familiar with the investigated phenomena. It is also useful when the researcher has a limited budget and time. Tuncalp (1988) reported that it is a difficult, if not impossible, task to draw a probabilistic sample in Saudi Arabia. The sampling difficulties are so acute that non-probabilistic sampling becomes a necessary evil. It is not easy to develop a sample frame of women due to the privacy and sensitivity of the Saudi culture. It is uncommon to ask about a woman’s address or contact information.

The researcher used a number of criteria to select the case companies:

- Company brand reputation and nationality: The researcher targeted companies that possessed the most well-known brands around the world.
- Location: This allowed the researcher to gain access to these companies and also ensured geographical diversity of the companies. Silverman (2013) mentioned that accessibility and convenience are grounds for guiding researchers in their selection of case studies.
- Company type: The researcher targets franchise companies operating in the restaurant sector.

- Cultural diversity: The researcher aimed to listen and interview different perspectives. He was also interested in interviewing companies that had different brand nationalities and from different categories (fast food, casual dining, high-end and fine restaurants) to enrich the study.

The researcher paid a visit to Saudi Arabia in July 2015 to check the environment and visited the chamber of commerce to obtain the blue pages directory that has the locations and contact information of Saudi companies. In addition, the researcher visited the biggest library in Saudi Arabia, the King Fahad Library in Riyadh, to look for more of information on franchising in Saudi Arabia. Before embarking on the study fieldwork, the researcher sent a letter to key people in the target companies via the university email, explaining the aim and the purpose of the study and the supervisor's contact information.

The first email was sent in March 2016, once the interview date was confirmed and arrangements made to conduct the first interview. Vassiliou (1980) stated that fieldwork is perhaps the hardest function of the primary research process, requiring a well-skilled pool of interviewers who should strictly stick to interviewing instructions. The researcher spent eight and a half months in Saudi Arabia for data collection and did not bother the participants during the Ramadan or Hajj season, which is the busiest season (traveling, fasting and performing Hajj) for the majority of people in the kingdom. Gorrill (2007) mentioned that Saudis are not punctual when it comes to business meetings compared to Western businessmen due to their obligations of praying five times a day and other religious holidays, such as Ramadan and Hajj.

The researcher relied on the blue pages directory to approach the companies. However, the blue pages directory was not clear and did not highlight which companies operated in the franchise fields, so the researcher relied on the internet and on visiting food courts in shopping malls in order to identify the key companies. The researcher contacted around 52 Saudi firms, either by visiting, emailing or phoning the company. The researcher managed to gain access to 31 companies, and the rest of the companies were either not interested or never replied. The researcher tested the questions in a couple of interviews to make sure the interview questions were clear and fully understood by the interviewee. The researcher tweaked some of the

interview questions that used marketing Terminology .Kvale, (2007) indicated that the pilot test will help the investigator to determine if the interview questions have errors, boundaries, or other flaws .This helps the researcher to take the nesseeccary measures to fix it before embarking on the study. The researcher found it difficult to approach Saudi companies because some had not updated their address or contact information. Tuncalp (1988) indicated that when conducting a study in Saudi Arabia, the telephone directories are not clear and out of date. There is no postal delivery of personal mail to homes. The postal system breaks down in rural areas, which make it difficult to approach Saudis in such regions. Leonidou and Rossides (1995) stated that there are problems related to conducting research in the Gulf States, such as reaching remote areas, unavailability of street maps.

The researcher paid a visit to shopping malls to visit the food court, where he was able to meet staff and introduce himself and the purpose of the study. It was a successful strategy, as the researcher ended up with business cards from the targeted people. When the researcher contacted them and explained the purpose of the study he was surprised by the welcoming attitude and willingness to participate in this study. The researcher was wearing the Saudi traditional attire. It has been suggested that while conducting cross-cultural research, insider researchers who share similar social, cultural and language backgrounds are better than outsider researchers in terms of speaking the same language as the interviewees; understanding local values, knowledge and taboos; knowing formal and informal power structures; obtaining permission to conduct the research; gaining access to records and easily facilitating the research process (Liamputtong, 2010; Merriam, 1998). The researcher, before the day of the interview, reminded the participants about the interview through WhatsApp message or call. Tuncalp (1988) mentioned that even Saudis who were interested in responding would require repeated reminders or call-backs. Time runs much slower in Saudi Arabia. Marshall and Rossman (1995) stated that when fieldwork should be concluded when recurring issues, behaviours and topics appear, as the point of data saturation has been attained. After carrying out of 45 interviews, the participants' answers appeared to be the same. The researcher decided to stop interviewing and not to seek out other Saudi companies, because the saturation point had been reached. As the researcher does not live in or close to the three major cities where the interviews took place, it would have been expensive to travel back and forth and stay in hotels. Eisenhardt (1989b) claimed that

“theoretical saturation” can be reached; likewise, Guba and Lincoln (1994) maintained that case selection continues until the point of “diminishing returns”. Daymon and Holloway (2002) stated that once the researcher can’t gain any new opinions, views or ideas from the participant interviews, the researcher has the option of continue or to stop the interviews.

#### **4.5 Data Analysis**

There are different strategies to analyse qualitative data, such as content, discourse, thematic and template analysis (Bryman and Bell, 2011). Thematic analysis is a strategy for recognizing, analysing and describing themes within data. It unifies and explains the data set in a rich manner. However, it also often goes beyond that and explains the different features of the study (Boyatzis, 1998). Qualitative methods are varied and complicated (Holloway and Todres, 2003), and thematic analysis should be perceived as a basic approach for qualitative analysis. Saunders et al. (2007) stated that researchers analysing qualitative data have to follow a procedure of categorization, unitizing data, recognizing relationships and developing categories and developing and testing theories to reach conclusions. In a qualitative study with large amounts of data, controlling and dealing with data in a precise manner is a challenge that has been studied extensively by scholars, particularly due to the large volume of qualitative data and the variations in reporting and being involved with the data (Bryman, 2012; Gibbs, 2007). Academics have managed to reach an agreement about the best ways to deal with and control the data. One of the solutions was the emergence of Qualitative Data Software, CAQDAS (Gibbs, Friese, and Mangabeira, 2002).

Braun and Clarke came up the following phases: *“familiarisation with data, generating initial codes, searching for themes, reviewing themes, defining and naming themes and finally reporting the results”* (Braun and Clarke, 2006, p. 87). According to Yin (2003, p. 111), *“examining case study research evidence is not easy because the strategies and techniques have not been well illustrated”*. The analysis of qualitative data is a learning process, developed intuitively through practice and application and not through the reading of texts and manuals (Denzin and Lincoln, 1994). Thematic analysis was adopted here for analysing the semi-structured interview data. Since the researcher was not experienced in data analysis, thematic



analysis appeared to be the easiest way and gave the researcher the flexibility to deal with data. Thematic analysis was used in this research to build themes from the data gained from the recorded data. According to Boyatzis (1998), thematic analysis identifies, analyses and reports patterns (themes) within the data.

Codes recognize a characteristic of the data that becomes appealing to the researcher and indicate *“the most basic segment, or element, of the raw data or information that can be evaluated in a significant means regarding the phenomenon”* (Boyatzis, 1998, p. 63). The procedure of coding is a segment of analysis (Miles and Huberman, 1994), as data is arranged into significant units (Tuckett, 2005). There are different methods of coding. Manually, the researcher can code data by taking notes on the manuscripts the researcher is analysing and highlighting possible themes. The researcher may primarily recognize the codes and then group them with other data that proves that code, but it is essential in this stage to ensure that all data obtained is coded and organized together within each code. This may involve copying obtained data from each transcript and organising each code together in different computers. If using a computer software, the researcher can code by labelling and identifying varieties of text within each data. The researcher does not know what could be relevant later and hence should save related data. A common criticism of coding is that the context is misplaced (Bryman, 2001). Through the reading process, the researcher can become familiar with the data.

The procedure of transcription, while it may be considered time-consuming, annoying and dull, can be an a good means to begin immersing oneself in the data (Riessman, 1993). Further, some investigators even claim that it should be perceived as *“a key phase of data analysis within interpretative qualitative methodology”* (Bird, 2005, p. 227) and acknowledged as an *exploratory* act, where significances are made, rather than a largely mechanical one of placing verbal sounds on paper.

In this research, the researcher used the following process for the data analysis:

- Saving the data on the computer and then listing each interview carefully and writing down everything that had been said during the interview, along with the time, date, name of the interviewee and length of the interview and the location
- The researcher translated the interview transcripts from Arabic to English and the translations were reviewed to ensure their accuracy and retain the real meaning, except for

transcripts of interviews that had been conducted in English, where the researcher listened carefully and wrote down everything in detail. The researcher read through all interview transcripts and took notes to better understand the interview and be able to code the data and identify related themes. Under the thematic analysis approach, the interviews were systematically coded and recoded, paying attention to details and previous theories, studies that have been carried out regarding the franchising field in Saudi Arabia. The researcher completed the thematic analysis manually and became familiar with the data set during the reading and listening processes. The researcher made a table and placed each question in the table along with the corresponding answer. Then, the researcher read the answers of each question more than once using a highlighter to code words or sentences that appealed to the researcher. The researcher then grouped similar words under one theme and some themes were divided into sub themes.

#### **4.6 Validity and Reliability**

The question of validity can be summarised as whether the researchers see what they think they see (Flick, 2007). Validity and reliability should be tested at the pilot stage of an investigation, before the main phase of data collection commences (Easterby-Smith et al., 2004). Moreover, Cavana et al. (2001) concluded that validity is concerned with whether the researcher has measured the right concept and reliability is concerned with stability and consistency in the research study. Coolican (1999) noted that the validity of the study can be examined by adopting at least one of four techniques – face, construct, and content and criterion validity. This study adopted face validity. The researcher was able to match the questions of the interviews with their objectives. To increase the validity of this research, the interview questions were carefully prepared, piloted and refined with the assistance of the researcher's supervisor. The researcher refrained from using academic terminology that might confuse the participants. In addition, in some cases, the researcher managed to conduct multiple interviews within one organization, which helped the researcher validate the data and highlight any contradictions.

The researcher left time between each interview to avoid influenced by the previous perspective of the participants and to be fresh. In addition, the researcher used multiple sources of data

collection, which led the researcher to triangulate. The researcher kept himself neutral and gave the interviewees the confidence to answer the questions truthfully. May (1997) indicated that the researcher should keep his own knowledge and let the interviewee flow to avoid being biased.

The notion of reliability relates to the extent to which any research tool produces consistent results when used repeatedly (Carmines and Zeller, 1979). Reliability indicates the dependency, stability, consistency, predictability and accuracy of the research (Burns, 2000). Coolican (2004) mentioned two different styles of reliability: external and internal. External reliability is related to the consistency and stability of the tests involved in a research study conducted on several occasions. This will indicate whether the data would provide similar findings if the research is conducted on several occasions and administered to the same interviewees.

In addition, Joppe (2000) defines reliability as follows: *“The extent to which outcomes are consistent over time and an accurate representation of the total population under study is referred to as reliability and if the results of a study can be reproduced under a similar methodology, then the research instrument is considered to be reliable”* (p. 1). However, this is not an objective of the study.

Internal reliability is related to the consistency and stability of the data collection tools adopted in the study. This determines whether the data collection tool is consistent within itself through checking that all participants answered each question in the same manner they answered the rest of them. In this research the interview, questions were designed to help achieve the research objectives. The researcher also explained each question to the respondents in order to ensure that all questions were answered in the same way. In some cases, based on the respondent’s request, the researcher sent the interview questions to the interviewee ahead of time. Furthermore, the researcher, at the beginning of the interview, explained the purpose and aim of the study and informed the interviewee that they could withdraw anytime without providing any explanation or not answer any questions they did not want to answer.

The researcher interviewed Saudis and non-Saudis to listen to different perceptions and beliefs and managed to interview companies within different restaurant categories, such as casual

dining, fast food and fine dining. The researcher did not ask respondents about their age or educational level, which might have made them uncomfortable and vulnerable. The researcher provided the respondents with a letter with the supervisor's contact information, contacted them through university email and handed them his business card, which had the name of the university and the position the researcher worked in. The researcher also brought the university ID card along with him to assure all participants that the study was only for academic purpose and had nothing to do with espionage. Finally, the researcher sent the transcripts of the interviews for validation to the participants to confirm that they accurately represented what was said during the interview.

#### **4.6.1 Limitations**

A number of restrictions applied to this study. Using generalizations from the results of earlier studies on Saudi Arabia can be both risky and confusing (Khushman, Todman, and Amin, 2009). The credibility of such generalizations would likely to be influenced by the features of the Saudi economic, socio-cultural, political and legal system (Siddiqui, 2008). The study was restricted to three major cities (Riyadh, Jeddah and Alkhobar city) in Saudi Arabia, focusing on restaurant sector. The study targeted people experienced in running international brands in the restaurant sector. The researcher was also limited by the amount of time available to spend in Saudi Arabia, since the researcher resides in the United Kingdom.

The study could be affected by the individual perspectives of the researcher (Miles and Huberman, 1994; Yin 2003). The researcher could not hear the franchisors perspectives because the majority of them were based abroad, and thus the study was limited to franchisees perspectives. The researcher could not interview many Saudi women to hear their experiences and points of view; only one Saudi female was interviewed. According to Nabaa (1984), most Saudi women are inaccessible to male researchers for direct communication. Almaney (1981) claimed that privacy and Islamic traditions in the Arab culture make it harder for the researcher to contact females.

The researcher found it difficult to interview the actual owner of the master franchisee because the social hierarchy in Saudi society makes access difficult unless you have a connection. Muna (1980) states that the open-door strategy among Arabs is very restricted. However, the researcher managed to meet one Saudi franchisee.

#### **4.6.2 Ethical Considerations**

Saunders et al. (2009) suggested that valid research requires the researcher to behave appropriately in relation to the rights of those who become the subject of the work or are affected by it. Furthermore, Saunders et al. (2007) and Blumberg et al. (2005, p. 92) stated that “*moral principles, norms or standards of behaviour guide moral choices about our behaviour and our relationships with others*”. When considering what constitutes an ethical approach to research, Anderson (2009) mentioned two principles that emphasise such an approach: the first being that the interests of all participants must be protected and the second that the individuals from whom data is gathered should be no worse off at the end of the process than they were at the beginning. The university requires researchers to conduct research in an ethical manner. The researcher explained to the participants the aim and purpose of the study and assured them that the data would be confidential. The interviews were conducted in line with the time that suited the interviewees’ schedule. All interviewees were informed that they could withdraw at any time without providing an explanation.

#### **4.7 Summary**

This chapter discussed the research philosophy such as ontology, epistemology and methodology and illustrated the main methodological considerations made by the researcher. In this chapter the research approaches such deductive and inductive had been discussed. In addition, the researcher explained and justified the choice of inductive approach. Moreover, the researcher explained and justified the used of case study strategy. The chapter also discussed the two main data collection methods – semi structured interviews and document evidence – that were adopted to collect the empirical data, detailing how these methods are appropriate for the study. The researcher used purposive techniques and sampling frame of this study has been justified. The

findings of this study has been analysed using thematic analysis. The validity and reliability of the study had been explained and justified by the researcher. In addition, the limitations of both the interview and the documents have been explained. Moreover, in this chapter the ethical consideration of the study had been explained by the researcher. In the next chapter, the findings of this study will presented.

## **Chapter 5: Findings**

### **5.1 Introduction**

In this chapter, the researcher introduces the findings of the empirical study. The researcher conducted semi structured interviews with 31 different Saudi companies that operate in the franchise field in the Saudi restaurant sector. These companies are located in different regions (Riyadh, Jeddah and Al Khobar city), although a majority of them are located in Riyadh. In total, 45 people holding various senior management positions were interviewed, including franchisees, general managers and operations managers, and accounted for many different nationalities – both Saudis and non-Saudis. All the participants but one (female) were males. The researcher managed to reach companies with the right to operate more than 70 international brands in the restaurant sector (fast food, casual dining, quick service and fine dining), although a majority of these brands concentrate on fast food category (quick service restaurants). These brands represent several different nationalities. A majority of the Western brands were American; however, French, Australian, New Zealand, British, Italian, Canadian and Spanish brands were involved as well. The rest of the international brands included South African, Turkish, and Lebanese, Korean, Jordanian, Thai and Emirati brands operating in the restaurant sector. Some of these companies have the right to operate multiple international brands either in the food sector or the fashion retail. In reporting the findings, numbers were used to identify participants to protect their confidentiality. This chapter explores the most significant findings. Five themes developed from the interview transcripts are illustrated in the sections below.

- The role of franchising in the development of SMEs
- The influence of religious considerations
- The influence of cultural considerations
- Legal and regulatory environment
- The relationship between the franchisee and the franchisor

These themes will be related to the objective of the research in chapter 6.

## 5.2 The Role of Franchising in the development of SMEs

The majority of the participants agreed that international franchises in the restaurant sector support SMEs in other sectors; for example, construction, transportation, advertising and importing. For example, respondent #1 commented on how local SMEs benefit from the international franchise:

*‘Many of small and medium enterprises owners see us as a reformer and coach, and we helped them grow the company, which will lead to recruit more people, and we helped them raise the awareness of having a high quality product. Our vegetables are locally sourced’.*

Respondents listed a diverse range of benefitting businesses. Respondent #6 argued that their company dealt with local companies to provide transport and housing for their company workers. Respondent #8 mentioned that the international franchising had helped support small businesses, such the property rental agencies, advertising agencies and exporting and importing companies, whilst respondent #25 indicated that the international franchising helped support small enterprises, such as water, real estate and maintenance companies. This respondent also claimed that their company had local food suppliers who supplied them with Halal meat along with other products with a short expiry date. For example, this company sourced fruits from a local supplier with better fruit types than the franchisor’s country of origin.

However, a few participants believed that international franchises did not help SMEs grow or expand their activities within the country. For example, respondent #13a claimed *‘McDonald’s in Saudi Arabia imports the plastic cups from abroad; it is less expensive and is not reasonable to ask a local company to make plastic cups, as they will be of high cost’*, and respondent #9c claimed that all materials used by their company were imported from abroad, including clothes. This respondent argued that both the parent companies forced them to obtain raw materials such as frozen dough from the parent company.



### ***5.2.1 Encouraging Entrepreneurship***

Respondent #19 claimed that the real support for entrepreneurs will be seen when the master franchisee gives sub franchise to the locals. The respondent claimed that their company did not give sub franchise because its management failed to train and follow up the business and did not study the areas requiring the new shops to open. For instance, respondent #10a stated that *'our company has been allowed to give sub franchises within a certain area, the west region of Saudi Arabia, but in general the parent company is not a big fan of giving sub franchises because of the difficulty of controlling and maintain the quality of the business'*. Furthermore, this investigation identified that all respondents except one had reported that international franchises motivated young Saudi entrepreneurs in terms of expanding their vision and enhancing their knowledge to start and run their own business. For instance, respondent #19 stated *'Approximately 80% of the Saudi entrepreneurs benefited from international franchises in the development of management skills and the process of trade exchange and I was one of these people who benefited'*.

Respondent #10a claimed that *'International franchising helped reduce the effort of starting new business, especially when it came to creating ice-cream ingredients'*

Respondent #9c also claimed that international franchises inspired the local entrepreneurs to run their own restaurants and helped locals develop their managerial skills and become decision makers. This respondent mentioned that their company supported Saudi entrepreneurs wishing to expand their local brands in the market by supporting them financially, technologically and helping them find the right supply chain management. For example, their company supported local brands through a 'business incubation' programme. However, this respondent also argued there was a need for academic training centres in the food sector to help Saudi entrepreneurs attend workshops on food safety and hygiene, teaching them how to open new stores, customer treatment and brand management.

Respondent #13a argued that the international franchises helped transfer experience. This respondent mentioned that he/she knew someone who ran international brands and then opened

his/her own brand. Respondent #21a commented, *‘There is someone who’s interested to be a sub franchisee for our brand. He has eight local shops and wants us to give him a sub franchise for our brand to assist him in developing his local restaurants and the transfer of expertise’*. In addition, respondent#3 claimed that international franchises not only stimulate the spirit of entrepreneurship in Saudi Arabia but also that studying and traveling abroad and exposure to the media helped.

A role in providing opportunities for women was also identified by respondents – *‘It led to the emergence of businesswomen as, you know, running restaurants were controlled by men in the past and, as you know, our company is run by a Saudi businesswoman’*. Respondents #12 and #2 claimed that international franchises helped in the emergence of businesswomen through the operation of food trucks by women in KSA. Furthermore, respondent #13a claimed that international franchises helped businesswomen emerge, especially after the government removed the restrictions on them to open a trade registry without the attendance of a male guardian. Respondent # 15 stated, *‘There is a Saudi businesswoman who runs her brand, Munch bakery, which competes with other international brands in the market’*. Other examples are, *‘There is a Saudi restaurant called Shatter, which introduces traditional dishes; this restaurant is run by a Saudi businesswomen’* (respondent #12) and *‘There is this one lady I know called Lubna who runs Burger King in Saudi Arabia’* (respondent #9a). Finally, respondent # 14 argued that international franchises do not directly support businesswomen. They changed their perceptions, which opened their eyes to start their own business and inspired Saudi women to run their business (respondent #28).

The exception to this generally positive view about entrepreneurship was respondent #14 who had a very different point of view – *‘The international franchise has not motivated Saudi entrepreneurs’* – claiming that the experience of Saudis in the field of entrepreneurship in its early stage is thus not a mature experience. The respondent suggested that Saudi entrepreneurs have to keep in mind that they might be a franchisor in the future, so they better take care of their business from an early stage so that they will be able to penetrate at least the regional market. Similarly, respondent #27 stated, *‘I do not know if the international franchise has led to the emergence of Saudi women entrepreneurs’*, and respondent #22a believed that international franchises did not support businesswomen.

### ***5.2.2 Technology Transfer and Innovation Enhancement***

The findings indicated that a majority of the companies in the restaurant sector have not benefited in a major way from the international franchise experience in respect of transferring technology to SMEs except following the franchise company system ‘know-how’ and learning the operational management mechanisms.

Respondent #13b claimed that there was a barrier in the transfer of technology in the restaurant sector due the availability of technology in the Saudi market. The respondent argued ‘*our company follows a global system Aloha that is used globally by franchise companies*’

Furthermore, respondent #2 argued that international franchises perhaps helped transfer technology back in the 1980s, when restaurants took orders manually instead of using electronic systems. This respondent argued that the international franchise may transfer technology in other sectors but not in the restaurant sector. Respondent #9b claimed that some international companies prevented them from sharing technological information with local companies to avoid copyright infringements.

However, a few participants reported that the international franchises did help transfer technology, for example, (respondent #14) through equipment for cooking, communications and delivery services. Respondent #8 suggested examples for the applications of booking where the guest could book their seats before arrival and available a fast Wi-Fi Internet service.

In contrast to their responses about technology transfer, all participant companies except one agreed that international franchising had a positive role through enhancing innovative thinking and creativity among the SME owners. For example, respondent #2 commented on how international franchises led them to start their own local brand saying, ‘*I have my own brands, and my company has the ability to operate restaurants within Saudi Arabia*’. According to respondent #25, international franchising has stimulated creativity and innovation in the local market and is referred to local companies that have been affected by the experience of international franchises; for instance, Dr. Café who claimed that he has made more money than Starbucks.

Some felt that the existence of international restaurants made it much easier for local companies to create their own brands. Respondent #17 recounted how their company created its own local brand from scratch based on Turkish cuisine. There was a lack of Turkish food concepts in the local market; so, they paid a visit to Turkey in an attempt to attract a Turkish brand. However, they realised that Turkish companies were inexperienced in the franchising field. This respondent stated *'Based on our previous experience of managing international brands, we came up with our own concept'*.

A clear motivation for creating a new local brand was the freedom from external control and royalty payments. Respondent #28 stated, *'Having your own brand could bring success to the company more than having international brands. As you know, it has low cost, no fees, and you can meet the local demand and desire without being controlled by another partner'*.

All companies have operational overheads, but respondent #27 claimed that it was better for them to start local brands, as this would increase sales and spread the overhead costs. Furthermore, this respondent argued that having a local brand would help them get rid of paying royalty fees, and they would no longer have to be controlled by the franchisor.

An exception to this position was respondent # 25 who expressed a very different point of view: *'International franchise did not stimulate creativity and innovation, but it is good for the new investor due to the lack of risk that is associated with franchise business.* This company had eighty years of experience in the retail and restaurant sector with the ability to manage 40,000 workers and run stores in different parts of the world, such as Russia and the United Kingdom.

### ***5.2.3 Skills Development***

The research identified that all respondents except one believed that international franchise companies stimulated the development of managerial skills among SME owners, such as the ability to make decisions, implement good inventory systems, run a business and use different styles of management. Approaches to management, management skills and practices were often found to be different to the existing approaches and practices found in the Saudi market.

Respondent #13b argued that international franchising had helped develop the management skills

of their company, especially by dealing with American franchisors who respected time, organisation of work and ways of training employees and providing daily and monthly reports by sharing financial information with franchisees around the world to stimulate competition. This respondent stated that *'the American franchisor were better to deal with than Kuwaiti franchisor. The Arabs are not straight forward and things are done by telephone conversations and not documented'*

Other illustrations of changed management practices were provided by respondent #11 who claimed that international franchising has helped their company make products, maintain their quality and find good suppliers. Furthermore, respondent #9c claimed that in the fashion retail sector, the parent company sent them goods, and their company learned how to display clothes, layout and design the shop floor and manage the outlets and warehouse. The company used a special system to monitor sales and exchange information so that the parent company would know how much had been sold and when to reload the next shipment.

Returning to the restaurant sector, respondent #10a claimed, *"International franchising taught our company on how to manage workers' movement in the kitchen and the distribution of the machines such as setting up the warehouse, cooling and the number of workers needed in the restaurants"*

In addition, this respondent mentioned that international franchises develop management skills and decision-making abilities among Saudis. Their company learned how to train their employees, offering courses and workshops to meet their needs. In addition, they learned how to manage their branches and analyse the market. Respondent#10b also indicated that local brands such as Pizza Maestro learned how to expand their product and increase their market share through the existence of international franchise.

International franchising has helped hone managerial skills of entrepreneurship according to respondent #15. This respondent argued that while some Saudi companies have had some experience in running a business, they lacked experience in certain areas, such as finance and administration. The longer term benefits of skill development and management experience were illustrated by respondent #17 who argued that the reason their company started its own local

brand had nothing to do with getting rid of royalty fees or meeting local customer demands; this move was all about improvements in the managerial and financial capabilities of the management, which started the business based on its previous experience in the franchising field.

The exception to this general positive perception was provided by respondent #7b who expressed a very different point of view: *‘International franchise did not help in improving managerial skills’*. This respondent, who worked in Saudi Arabia for thirteen years, claimed that it depended on the individual and the company. This respondent argued that their company was simply following the systems and standards set by the parent company and was not an initiative towards skill development.

Similarly, respondent #22a argued that whilst some international franchises simply exploited their brands to gain profit, *‘International franchising has helped transfer the knowledge and the experience to the local market and promote business leadership. Some of the franchisors are exploiting the company’s name and reputation to gain profit abroad’*. This respondent argued that some of the local restaurants were much better in the Saudi market than the international ones. For example, respondent #2 indicated that Albaik restaurant, which is a local brand, is preferred to Kentucky Fried Chicken.

Finally, participant #12 raised an interesting point on how Saudi women were impacted positively by the presence of international franchising in the local market by saying, *‘International franchises helped develop managerial skills of managers, especially businesswomen who have now become decision makers and have the ability to run their business; they represent the board of directors of our company’*. This respondent claimed that women can sell their products from their homes – ‘productive families’ – and this has appealed to small business owners who have started dealing with families, especially those with high standards in terms of hygiene and quality.

#### **5.2.4 Providing Employment**

All participants agreed that the presence of international franchises in the restaurant sector played a very small role in recruiting Saudi citizens, and this varied from one region to another. They reported that most of the Saudis prefer to work in administrative positions rather than restaurants, interacting with customers. For instance, respondent # 3 stated, *'We found it difficult to recruit Saudis because of the nature of the work, such as baking and cleaning the kitchen'*. Respondent #13a argued that their company hired two Saudi's who refused to deal with the customer and preferred to work in the kitchen. Respondent #26 argued that many Saudis preferred working in the delivery service so that they could use the company's car for personal matters, and some of them liked looking around other people's homes when delivering food. Respondent #17 claimed that it is difficult to recruit Saudis because of this social outlook. Saudis see working in a restaurant as a temporary position, not a permanent job. In addition, respondent #13b argued that the social perspective towards working in restaurants started changing two years ago; however, many Saudis still look down on this position and prefer to work in the government sector. This respondent claimed that Saudization had succeeded in other sectors such as the telecommunications and banking but not in the restaurant sector.

Respondent #15 confirmed there is a difficulty in hiring Saudis. The company offered incentives to keep Saudi employees – for example, monthly and yearly bonuses – and have an ideal employee for the month and year. Respondent #30a claimed that Saudis do not like to be controlled by foreign managers. This respondent also indicated that their company gave almost 3,000 Saudi Riyals and tried to attract Saudi students by giving them flexible working hours, which would not conflict with their lectures.

Respondent #9a argued that in their company, which operates in the field of restaurants and fashion, used to have 3500 employees, including 900 Saudis; however, only about 5% of them were still working with their company: *'The international franchise have played a small role in the recruitment of Saudis in the restaurant sector, where the percentage of Saudization does not exceed 15%, and many of them prefer to work in the coffee shop instead of restaurants for the nature of work of being easy task compared to the restaurants'*.

Respondent #26 claimed that the Saudization rate in their company was 7%, and most of the Saudis worked in the sales department with a salary of 5,500 Saudi Riyals. This respondent also confirmed it was difficult to hire Saudis in restaurants because of the long working hours and physical effort. This respondent also elaborated that there were three branches of their restaurants run by women in different female universities in Saudi Arabia, but most of these women were foreigners. Respondent #9a mentioned that *'We tried to keep the Saudis through providing good training programs along with other incentives, for example, if the employee continues with the company for three years, he can get a car loan without interest, and if he continues for five years, he can obtain an administrative loan without interest, but the majority of them quit unless they feel forced to stay because of their financial situation'*.

Respondent #8 claimed that there are Saudis who left working in restaurants because they got government jobs. However, respondent #27 argued that the difficulties of life force many young Saudis to accept this kind of position and not rely on their fathers for money; therefore, they need to take full responsibility in looking for jobs.

Respondent #21f stated that the percentage of Saudization in their company is 21%, but it is costly to hire Saudis compared to another nationalities such Philippines; furthermore, they said that it is hard to retain Saudis after training them. Many Saudis were not fluent in English and did not like to clean tables. Respondent #2 argued that their company experienced difficulty in recruiting Saudis fluent in English to take orders from foreign expatriates. Respondent #31a also mentioned that Saudi women preferred foreign employees because foreigners were easier to deal with than Saudis. Interestingly, this respondent insisted that customers must also be educated to accept Saudization. Respondent #24 claimed that it is hard to find Saudis with an experience of working in the restaurant sector and, even if found, some of them do not show up on time. The respondent argued that their company created specific cashier positions to attract Saudis to work in the restaurants instead of 'multi-tasking' crew positions. However, respondent #28 claimed that there is a problem hiring Saudis with skills in cooking and waiters who know how to serve food; so, their company signed a contract with the Al hokair company to provide it with Saudi professionals. In contrast, respondent #27 claimed that there is no difficulty in finding competent Saudi workers due to the changes in the culture of work and education.



However, respondent #9a also indicated that the acceptance of working in the restaurant sector varied from one region to another; for example, in Al-Hasa and Al-Qassim, Tabuk and Taif city, the level of acceptance is high compared to Riyadh and Jeddah because the parents in these regions have carried out similar jobs in the past and did not feel ashamed of doing them. The same respondent claimed that there was a mall in the city of Al-Ahsa where the percentage of Saudization was 100%; however, their company brought this figure down to 70% because there were employees who had relatives working in the same shopping mall and covered up for them, and some of this staff who did not attend work because of their relatives, who they worked with, never reported this to the company. Respondent #25 argued that it was difficult recruiting Saudis because of their social outlook; however, the attitude towards working in restaurants is better in the Eastern and Western parts of Saudi Arabia, unlike Riyadh. This respondent claimed that many Saudis prefer working in big cities, as they are less likely to be seen by one of their relatives there. This respondent claimed that their company offered part time positions to give young Saudis a chance to try what it feels like working in restaurants.

From a different perspective, respondent #1 argued that international franchises increased the social acceptance of working in restaurants due to their big brand names, and respondent #12 claimed that international franchises reduced the culture of shame in terms of working in the restaurant sector. For example, respondent #14 claimed that many Saudis prefer working in international companies, such as Pizza Hut and KFC, compared to working in local restaurants.

Based on these findings, it can be said that the international franchise has positively led to some areas of development in the Saudi economy. There are strong relationships between international franchise and the development of SMEs. It has helped SME owners in transport and maintenance and advertising companies improve their business activities by increasing their supply and distribution channels within the country as well as educate them about the importance of having good quality goods. In addition, international franchise has helped SME owners improve their managerial skills by providing good training and workshops on how to manage their financial budget, finding the right supplier and recruiting staff. It has also helped them build on their communication skills by dealing with international franchisors, respecting their time and communicating effectively with their employees. International franchise has also helped the Saudi entrepreneurs run their business and become more creative and innovative by creating

their own brands; it also educated them on how to manage and run different branches within the country and penetrate different regional markets. Local entrepreneurs learned from this model, becoming more self-determined decision makers and the importance of team work.

In addition, this empirical study found that international franchise did not help transfer technology in the restaurant sector due to its availability in the local market and because of some international franchisors setting conditions for not sharing their system with other companies. Furthermore, this research identified that international franchises did not help reduce the unemployment rate in Saudi Arabia due to cultural considerations. For example, many citizens do not consider working in restaurants as a permanent job, and the social acceptance towards working in the restaurant is seen by the interviewees as a challenge that needs to be addressed. The percentage of Saudization rate is low indicating Saudis still resist working in the restaurant sector

### **5.3 The Influences of Religious Considerations**

For most foreign franchising companies, the influence of religion may be seen as a potential barrier may lead to adaptations of the standardised business model that is core to the franchise concept. However, there was a common sense amongst respondents that religion is not a major issue for the international franchisor's brand in the Saudi market.

#### ***5.3.1 Halal Product and Alcohol***

Some of the respondents claimed providing Halal meat is not an issue to the international franchisor. For example, respondent #1 said, *'The franchisors are aware of the difference in culture and religion in Saudi Arabia. For example, our brand depends 20% on selling alcohol and 10% on selling pork but, here, in Saudi Arabia, our meat is Halal, approved by the Saudi government and in compliance with sharia law'*.

Respondent #10a claimed that their company sourced meat from the local market to avoid problems; contrarily, respondent #9a stated that *'Due to the difficulty of obtaining good quality*

*meat from the Saudi market, our company used to get meat from Spain, and this had been approved by the Saudi Food and Drug Authority'*

Respondent#29 claimed that in 2015, the South Korean parent company gained a Halal certificate to avoid problems while respondent# 1 claimed that their company replaced alcohol with fresh juice and coffee with the current sales of beverages being 20%, which is equivalent to the sales rate of alcohol in the parent company. This respondent noted that the parent franchisor supported their company, providing flexibility to meet local needs; therefore, the company excluded alcohol from food recipes and replaced pork with lamb or beef.

Respondent #14 claimed that in the hospitality sector, international hotels sold alcohol in all countries except Saudi Arabia, and that did not affect sales. Respondent #9b stated that their company replaced the bar section of one their restaurants with a special section for pastries and wines and alcohol with juices. Respondent #9c mentioned that their original restaurant concept is based on music and selling alcohol and that their brand relies heavily on selling wedding cakes and alcohol. However, in Saudi, they focus on coffee drinks. The respondent stated that the parent franchisor has no problems because of the large size of the Saudi market. Respondent #17 argued, *'As you know the Saudi market is profitable and good chance for international brands to boost their brand's reputation, so they need to respect the country rules and regulations'*

### ***5.3.2 Gender segregation and Restaurant Design***

Gender segregation is not an issue for the international franchisors when designing the restaurant. A majority of them adapted their restaurant design to country's religious customs and are familiar with the religion. Respondent # 1 claimed that the franchisors are aware of the differences in culture and religion of the country and the need for a family section requiring an increase in area of about 20-25%. However, respondent # 25 stated, *'There was a challenge for our company at the beginning stage to explain to the franchisor the opening of two different sections, a section for the families and singles'*. Respondent # 6 also stated that a franchisor of one of their brands was surprised when they heard of a section for families and singles but now is used to it. Respondent # 13a claimed that they contacted the parent company about the design of the restaurant and explained how this is could be done by creating a partition wall that would

prevent singles from seeing families section. Then, words were exchanged with the designers, explaining the purpose of the design. The designers emailed the respondent back saying that the staff in the back of the kitchen could still see the family section. The respondent did not know how to explain that Saudis weren't supposed to see, but it was okay for foreigners.

However, respondent #10a indicated that opening separate family and single sections is costly, and respondent #5 placed a 50% premium on these sections. Respondent #8 noted that having male and families section also required an increase in the number of employees in the family section. Respondent #10a argued that having a family and singles section required 25% increase in the size of the property: *'When it comes to the family and individual section, we have two of the largest restaurants in the world because they contain the family and individual section'*. In contrast, respondent #27 claimed that having an individual and family section was not expensive because their company had prepared and agreed upon a budget. Customer needs were needed to be met with. The franchisor would send a file containing a selection of pictures, and they could choose what would suit the Saudi culture and what would the franchisor best be familiar with regarding the religion of the country.

Respondent #9a claimed that almost 70%–80% of the profits in their restaurants came from the family section. The respondent stated, *'In one of our restaurants, there was a special section for singles and families; but due to the lack in the of number of men and increase in the large number of families, we made it a family section'*.

In addition, respondent #16 claimed that their company did not face problems when it came to gender segregation because most of their international restaurants belonged in shopping malls. Respondent #17 argued because the family section was on the second floor, there was no need for extra property. Furthermore, respondent #7a claimed that international franchisors were now familiar with the Saudi culture, especially when it came to male and female segregation. This respondent argued that in their restaurants, they did not have a family section because women were allowed to enter and order but not allowed to sit inside the restaurants.

Furthermore, this research identified that a majority of participants did have a partition wall in the family section and this does not affect their business or the franchisor. In some cases, a

flexible solution was offered. Some companies did not have a permanent partition wall unless the customer asked for it. For example, respondent #15 indicated that customers dined in an open area because their restaurants were targeting a certain category of customer. A majority of the customers had no problem with this arrangement, but there were some who requested for a partition wall for privacy. Respondent #12 claimed their restaurant also did not have a partition wall in the family section but could provide a partition wall if the customer asked for it. Respondent #1 observed that a partition wall is requested more often by the locals in Al Qassim city than in their branch in Jeddah city because there are many different nationalities in Jeddah compared to Al Qassim city. Moreover, respondent #20 stated, *'When it comes to the wall partition in family section, we do have 60% of our restaurants, where the families can dine in an open area, and 40% of our restaurants, where the families can dine in private space'*.

### ***5.3.3 The prayer time***

A majority of companies claimed that the closure of their restaurants during the prayer time does not affect their business operations, sales and productivity and should not be considered as an issue for the international franchisors. For instance, respondent #11 stated, *'The closure of stores during prayer time, I have no problem as long as the other shops shut down and consumers are aware of the purpose'*. Respondent #17 stated that their company is careful not to cook ten minutes before prayer time, and customers are not allowed to sit inside during the prayer time. Customers are informed ahead before the call of the prayer. However, respondent #8 claimed that customers are allowed to stay in the restaurant during prayer time but are not served then. In Madinah City (holy city), they do not let customers stay inside the restaurant during prayer time and so notify them half an hour ahead of the prayer time, unlike in other cities where customers are permitted to sit in.

Respondent #20 also claimed that closing during prayer time does not affect their sales and operating the business. It is seen as a positive thing to give staff members the right to perform prayers as a sign of respect, and this will be reflected in their willingness to do their best. Respondent #9c states, *'I think it is break time, which will lead the staff to smoke and drink coffee or perform pray'*.

Respondent #7a argued that their company has no problem closing shops during prayer time as long as the customer is accustomed to the system; they also said that many prefer to come after the end of the last prayer. The respondent stated, ‘*As you know, the customer can return after prayer if he/she wants to buy something*’. Moreover, respondent #1 argued that this adaptation is important to meeting social requirements in all cities in the country. This respondent claimed that their company had segregated areas for men and women for prayer time. Respondent #10a claimed that customers are aware of closing times, so many of them might come earlier before the call for prayer or after the prayer; some customers do show up during prayer time and do not want to wait; so, they decide to leave. However, their company trained its employees to deal with prayer times.

Respondent #24 noted that their company kept the oven on during closing time to avoid any problems, as customers were not patient enough to let them reheat. Respondent #3 claimed that some of the food under preparation could be affected and spoiled and, so, some of the staff was needed to stay inside the store to keep eye on it. Respondent #25 claimed closing the shops during prayer time was not problem for the franchisors, and the Americans were understanding compared to other foreign franchisors.

However, a few companies claimed that shutting down restaurants during prayer time effected their sale and the operations of their business. For instance, respondent #13a claimed that during prayer time, they let customers sit inside the restaurant to finish their meals but stopped serving. This respondent argued that the length of the time between the call of each prayer and the end of it is between 20–30 minutes. During this time, the customer may need to order something, ask for a drink refill or complain about what he/she is eating and want to order something new. In this case, many restaurants can make money and appease customers with good service. The moral police<sup>8</sup> forced them to close their restaurants 10 minutes ahead of prayer time, which prevents many customers from ordering: ‘*I personally am against the closure of shops during the prayer time*’. Respondent #9a argued that closing during prayer time affected their sales. The

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<sup>8</sup> Is formally known as the Commission for the Promotion of Virtue and Prevention of Vice. In 2016, the Saudi government stripped its religious police of the power to arrest when carrying out duties and enforcing Islamic law. They no longer detain people they identify as breaking the kingdom's strict standards of moral conduct. Now, they must report individual ‘misbehaviors’ to the police.

total length of the prayer time is four hours a day, but they have to follow the system of the country. This respondent argued that their company was able to compensate for its loss after the evening prayer. It would reduce the number of workers during daytime and increase the number at night due to the increase sales and the number of its customers. Respondent #12 claimed that closing shops during prayer times affects sales, as customers cannot enter the store then. This respondent stated, *'I think it is a good idea if the customer is allowed to get in, and they can pray instead waiting until the opening of the stores, especially women'*. Respondent #6 claimed that closing during prayer time may affect the business; so, their restaurant takes the last order half an hour before the call for prayer. This respondent claimed that their restaurant prepared the food fresh; so their company changed the design of the kitchen. It turned the display area from the front of the kitchen to the back in order to avoid throwing away food and maintain control.

Finally, one of the participants (#30b) raised an interesting point by saying, *'Sometimes I feel hungry, but I have to wait until the end of prayer. I have some reservations about closing restaurants during the prayers, especially the closing of the important shops'*. This respondent argued that the same law should be applied to all other government sectors. It was argued that as all the restaurants are closed during the call of prayer, there is no restaurant open to compare the impact on sales.

#### ***5.3.4 The Holy Month of 'Ramadan'***

All the companies agreed that the sales of their restaurants dropped in Ramadan, and this made the international franchisors allow the franchisees to add local dishes, which might affect their brand standard. A majority of the companies tried to promote their sales by adding dishes despite sales being down. However, the sales fell down. For instance, respondent #1 claimed that sales were reduced in Ramadan by almost 25%, as the restaurants were closed for almost ten hours per day and open from 6.30 p.m. to 2.30 a.m. Restaurants offered an open buffet for 'breakfast meal' that included Middle Eastern food to promote their sales. Furthermore, respondent #2 *'During Ramadan sales fell by 70% especially during the first two weeks of Ramadan, and then started to pick up a little bit during the last days of Ramadan when people were getting bored of the traditional cuisine'*

Respondent #13a claimed sales fell by 90–95% during the holy month, especially in the first ten days and there are also lower sales in the Hajj season. Respondent #3 claimed sales fell in Ramadan and during rainy weather but increased during winter sales because people like consuming hot drinks then. Respondent #5 claimed that sales fell in Ramadan by 35–40 % in all brands except one restaurant, so their company added some varieties of food to its menu, such as samosa, dates and soup, and reduced its meals' prices. Their franchisor had no problem with this.

Sales fell by about 30% in Ramadan, and this percentage varies from one restaurant to restaurant according to respondent #6. They went on to say that one of their American restaurants was doing well in Ramadan, so their company tried to attract customers through breakfast promotions and added lentil soup and dates to its menu. Respondent #9a stated *“Sales fell in Ramadan by 60% to 70% and this also varies from one restaurant to another. For example, sweet and pastry shops may not be as badly affected as other restaurants due to the Eid season”*

This company added Arabic coffee and dates to promote sales and made other amendments. For example, for one of their restaurants, they offered breakfasts and Suhoor meals so that they would not have to add anything to the menu except berries drink and Arabic coffee. In contrast, this respondent claimed the sales of their fashion retail stores increased in Ramadan because of the festival of Eid.

Respondent #10b claimed sales go down by 70% in Ramadan, and the franchisor does not have the flexibility to change the menu; so, their company tried to offer a bundle of meals at a reasonable price to promote sales. Their company focused on the Suhoor meal, having the meal before the dawn, and sometimes served blizzard ice cream with dates and Baklavoh.

Respondent #16 claimed sales dropped by 50% during Ramadan. The Lebanese franchisor is more flexible compared to other Australian franchisor in terms of adding different varieties of dishes to the menu during Ramadan. For example, in Ramadan, they add dates, Arabic coffee and Basbosa (Arabic desert). Respondent #18a claimed that sales go down in Ramadan and during summer holidays because Saudis travel abroad during this period. During Ramadan, sales drop by 5% to 10% in the restaurants operated by respondent #25 whilst those in the coffee shop



increase despite closing during daytime. People like to consume coffee after Iftar<sup>9</sup>. This company added dates to the menu and offered deals at a lower price. New to the market, finally, respondent #28 claimed that their company had not experienced Ramadan and did not have a plan; neither had they discussed it with the franchisor.

### **5.3.5 The Moral/Religious Police**

All the respondents claimed that they had not encountered any specific issues with the religious police and did not affect operating their business. For example, respondent #3 stated, *'We never experience a problem from the religious authority. They stop to remind us of prayer time'*.

However, most respondents gave examples of incidents as interventions that had impacted their businesses. Respondent #2 claimed that their company had a good relationship with the religious police; he, however, said, *'I have suggested them to not stop their car in front of the entrance of the restaurant, as the sales will go down by 50%'*. This respondent argued that customers feel uncomfortable seeing the religious police car parked in the front of the restaurant, as they do not want to get into trouble. Some of the religious police might enter the family section to ensure no woman is dining with her non-relative males and advice not letting people dine in open areas. However, this respondent argued that dining in a closed area will encourage some female customers to dine with their non- relative males.

Some customers stay inside during the prayer time to finish their meal, some want to leave to attend prayers and others just get bored; so, the staff may get caught by religious police when they open the door for customers to leave the restaurant during prayer time. Respondent #8 argued that it is hard to satisfy both the customer and the moral religious police. Respondent #9a claimed that their company never experienced problems with the religious authority in the restaurants but had faced problems in the retail sector regarding women's clothes and graphics as well as the mannequins used along with imported bags. Sometimes, goods enter the market by

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<sup>9</sup> Breakfast Meal or 'Iftar' is the evening meal that Muslims have after ending their fast at sunset.

mistake and violate country rules. This respondent claimed that sometimes, the religious police ask them to take the mannequins out of the scene. Respondent #10a stated that their company does not have any problems with the religious police but claimed many of them do not like their company serving cakes for Valentine's Day and birthday parties and have thus asked them to remove them. The parent company catalogue contains these offerings but replaced them with special cakes for the Saudi National Day. This respondent mentioned that their company used to hire Saudi female cashiers in its restaurants but stopped hiring women because of the religious police.

There are other examples of intervention. Respondent #22a indicated that some religious police asked them to remove pictures that showed faces. Respondent #4a claimed that the religious police would sometimes take their staff to the police station because of staying longer for cleaning and closing down. Respondent #18a claimed that the religious police pay their restaurant visits on different occasions. They usually request female customers to cover their faces or their hair. The role of the moral\religious police is variable. Respondent #7a claimed that their restaurant celebrated birthday parties for children, and the religious police seemed to have no problems with it. However, respondent # 5 claimed that their company used to offer birthday parties but, because of the intervention of the religious police, they stopped. This respondent also mentioned that some of their staff had been deported. This respondent claimed through their experience in running their restaurant that the moral police in Alqassiem city is more pragmatic and more tolerant compared to the ones in Jeddah city.

Respondent #20 claimed that the religious police prevented them from hanging a portrait of the brand owner's mother on the restaurant wall. However, their company kept in touch and contacted the religious police in advance to attend the grand opening of its fashion retail brand in order to prevent the mingling between genders. Respondent # 21d claimed that one of its restaurants has separate entrances for males and females. They recalled that once a woman was sitting in their store, and the religious police had asked them to place a sign indicating that women were not allowed to sit inside the store. Moreover, respondent #25 claimed that their company has had to sometimes confront the religious police; for example, when they were asked

why people were celebrating birthday parties and told to stop the music<sup>10</sup>. Finally, respondent #30b claimed that their restaurant has a single line for both male and females, and the religious police commented on the presence of a single line. The religious police do not like the idea of having one line instead of separate lines for both men and women; however, their company can't make two lines because of the small area of the restaurant. Contrarily, this respondent claimed that the religious police understood this. However, respondent #15 claimed that they play music in all their restaurants softly. There is resistance from some customers, and the attitude towards the music varies from one city to another. This respondent also stated, *'As you know, the religious police do not encourage it'*. Respondent #22b recalled this one time when the music was playing in their restaurant and one of the restaurant's customers who was dining reported this to the religious police. Respondent #12 mentioned that their company plays soft music in the family section of their restaurants. The company make sure that the music does not intervene with the call for prayer. Some customers enjoy the music, whereas some ask to shut it down. This respondent stated, *'The religious police asked us a couple of times to stop playing music'*.

In contrast, respondent #13b considered religious police as a hurdle to the provision of good service and running business. This respondent stated, *'As you know, the only thing separating the family and the singles is the cashier counter in our restaurant – which is a partition; so, the moral police asked us to change the men's and women's cashier counters; so that increase the cost'*.

This respondent also mentioned that the cashier in their restaurants usually shouts loudly when a customer places an order – for example, 'one burger' – and then the staff in the back kitchen repeats the same loudly – 'One Burger' – as a way of fun. The religious police prevented them from doing this. In addition, the moral police got involved and intervened with some of the restaurant staff's dressing sense or styling of hair.

Based on the empirical study, religion is not a major issue for the international franchisor; most of international companies are aware of the influence of religion and have made some amendments to their operational manual to adjust to the religion. For instance, in the case of providing Halal, companies managed to place pork with beef or lamb and replace alcohol with

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<sup>10</sup> Recently, The Saudi General Authority for Entertainment allowed live music show and stand up comedies in cafes and restaurants across the country.

juices. International companies designed their restaurants in accordance with the religion of the country through the provision of a male and family section. In addition, franchisors adapted their operational manual to deal with the closing of the outlets during prayer time, such as training employees to deal with customers and praying time. Religion may require additional adaptation cost but not barrier for the international franchisor to penetrate the Saudi market. However, Ramadan appears to be a seasonal challenge to the franchisor due to low sales and the difficulty in changing the lifestyle and eating habits of the people either by adding dishes or promotion by offering a bundle of meals at a lower price.

#### **5.4 The Influence of Cultural Considerations**

A majority of the participants insisted that culture is not an issue for the franchisor brand to enter the Saudi market. For instance, respondent #4a stated that *'The franchisor has visited Saudi Arabia to see the culture and know about the country customs and has no problem with it'*. To address the issue of cultural understanding, respondent #25 indicated that their company usually invited international franchisors to Saudi Arabia to illustrate how lucrative their market is and how much their country has to offer. Some of the international franchisors commented positively after their visits, especially Americans. This respondent stated, *'Some international brands refused to enter the Saudi market, especially in the field of fashion retail; the brand operators had a political agenda against Saudi society as being closed and stereotyped the country being a desert country with camels'*.

Respondent #9b claimed that their company never experienced any resistance from any international brand except the American brand 'Chipotle'. They claimed that the company wanted to focus on Europe and Russia before penetrating the Middle Eastern countries. In addition, respondent #1 claimed that the franchisors are aware of the difference in culture of the country. Respondent #7a claimed that their company had asked the international franchisors to pay a visit to the country to know more about the Saudi culture and tradition. For example, respondent #2 from a Japanese restaurant claimed that in the Saudi society, it is not acceptable to let two families sit next to each other on the same table. Their company has extended the size of the restaurant and come up with a solution. If the family size is too small (e.g. two people), they

have the option of either waiting for the next available table or go upstairs where one chef cooks for all the customers. In addition, respondent #29 stated, *'The Saudis love comfortable chairs; so, we change the size of the chairs, unlike Koreans; they prefer wooden chairs. They do not mind strangers sitting next to them unlike in Saudi Arabia'*. Furthermore respondent #10b mentioned their company had added a home delivery service because women cannot drive in Saudi Arabia. They ensure the delivery bag is set at the right temperature to maintain the quality of the product and save it from germs. This respondent claimed the franchisor had no problems with the offering of this service, even though this is not available in the United States.

Some of the participants consider the language of the country as a challenge for the international franchisor. For instance, respondent #29 stated, *'As you know, Koreans do not speak English. They are proud of their language. There is an English translator for the franchisor, but there is difficulty in transferring the idea and a delay in responding to the email'*.

Respondent #9a mentioned there is a language barrier between their company and the Turkish franchisor, and there is a difficulty in transferring knowledge to the Saudi market. Their company hired people who spoke both Arabic and Turkish to avoid any problems. However, similarities between the cultures and customers' tastes helped their company save time in terms of adapting to the local market, as the Turkish tastes were close to the Saudi tastes. In addition, Arabic language was a challenge for franchisors according to respondent #4a, as the employees of the local companies and government organisations did not speak in English.

According to respondent #13a, one of the reasons why their company focuses on big cities is culture. For example, if they opened their restaurant in the North (e.g. Arar city and Tabuk city), they feel some people there would still not be used to eating burgers or might consider it shameful to hangout or invite friends to have a burger and would not want to pay a higher price for a gourmet burger.

Another common cultural issue according to respondent #8 was that the work ethic in the West is different from Saudi Arabia. There are difficulties in Saudi Arabia, but they have overcome it. For example, their company trained its staff not to talk to women and speak to the male relatives only as well as not make direct eye contact with or smile at women. Respondent #28 also

mentioned that their company trained its employees on how to deal with men and women and keep a distance: *‘As you know, some of our staff are Philippines. They do not know the reason for the separation and the partition wall in the family section’*. Respondent #18a claimed their company has hired Western expatriates to work in the restaurants, and it is hard for them to cope with the differences from their own culture.

#### ***5.4.1 Product Adaptation***

A majority of the participants claimed that the international franchisors modified their brands to suit local preferences, tastes and demand of the culture. According to respondent #6, their company asked the parent company of a British brand to increase the portion size, as the Saudi customers preferred larger portions of food. In addition, this British parent company was also asked to offer cooked instead of raw seafood. This respondent claimed there was some resistance from the parent company, and it eventually agreed to their request; so, the customer now has two options: have raw food or cooked seafood. Furthermore, this respondent stated, *‘The American franchisors are more flexible when it comes to the adaptation to the culture than the British franchisor in terms of accepting new ideas. For example, the Americans helped us develop a special menu for Ramadan’*.

Respondent #28 noted that their restaurant provides a small sauce box with meals in Jordan contrary to Saudi Arabia that has increased the number of sauces available based on the customer demand. Respondents #12 mentioned that their company has modified cooking steak so they that they can serve a medium-rare and well-done steak.

Some of the international restaurants struggled to succeed or had limited success in Saudi Arabia due to cultural reasons and consumer behaviour. Respondent #1 claimed that although they have 65 items on the menu of their American restaurant, customers keep ordering cheeseburgers each time they visit because several hamburger brands have penetrated the Saudi market, and this has become a habitual trend. They came up with idea of using the slogan, *‘If you do not like what we offer, it is for free’*; within four months, customers started ordering different items from the wider menu. Furthermore, although they were able to hire a Saudi female as a hostess in their

restaurant in Jeddah, it was hard to hire a female hostess in the family section in Al Qassim city due to the (lack of) culture acceptance.

Respondent #19 also argued that when Taco Bell opened in Saudi Arabia, it did not succeed because its consumer eating habits are different from that of Americans. Saudis are not big fans of eating wrapped beans with rice. In addition, respondent #10a claimed that consumer habits in Saudi Arabia are different from what they thought: *'Our signature is the blizzard ice cream, but 80% of our sales come from selling meals and 20% from selling the ice cream'*. Regarding their product matrix, they thought it was 50/50 of the percentage of sales. This respondent argued this is because people in Saudi Arabia like to eat outside, especially the young ones.

Respondent #15 claimed there was a difficulty in accepting the brand; for example, in their American Mexican restaurant. The fondue cooking method, a Swiss method of preparing food developed by the Americans, takes a long time to prepare food, and the Saudi customer does not have the time to spend two hours in the restaurant. This respondent claimed their restaurant adapted this cooking method to reduce the amount of cooking time, and this process had been adopted by the parent company in the States. In addition, this respondent claimed there was a difficulty in promoting Asian food; so, their company adapted to the product to suit the local taste. For example, they replaced spring rolls with samosas, sweet chilli sauces were modified and the sweet and sour chicken was modified by increasing the level of sugar to meet the customer's taste.

Other menu adaptations included addition of chicken pizza to meet Saudi consumers' desires, even though it does not exist on the menu of the original company (respondent #11). Respondent #10b stated *'we excluded some dishes that had a low demand such as coconut ice cream and the fish sandwich and instead we added kofta sandwich with tahini'*.

They deleted some oriental sweets with Korean roots from the menu, such as crushed ice, and added some touches on pastries, such as black seed, thyme and liquid cheese, to make it appealing to the locals: *'we spent a year and a half for the adaptation'* (respondent #29).

Respondent #16 claimed their company reduced some food salt to adapt to the customer taste while respondent #17 claimed their company added a shrimp appetizer to their Australian brand, which was approved by the franchisor and excluded the sauces mixed with alcohol and three other sauces due to the lack of demand. Respondent #24 indicated that their company served

Nutella and tortilla sandwiches and some chicken sandwiches in their outlets, and the parent company representatives did not mind that, although they were tested to make sure they met the parent company's standards.

Finally, respondent #13a indicated that their company provided a server who serves the customer, a service not found in the restaurants of the parent company, and also added appetizers to the menu and removed burrito because of its lack of demand. In addition, although the interior design is the same as that of the parent company, the exterior is different. Marble was added as the Saudi customer loves luxury things. This respondent claimed the franchisor is flexible as long as their company understands the main concept. In addition, respondent #15 claimed that their company added to the design of its restaurants iron cages, some stones and also luxurious animal leather wallcoverings and bright colours as long as this did not affect the main concept of the parent company's design

In contrast, the participant from company # 5 stated, '*We have not done any modifications to our brands to meet the customer taste*'. Respondent #25 argued that their company did not modify its international products to adapt to the local culture. This respondent argued that the local people wanted to experience something different. A point is echoed by respondent #1, '*It is a nice thing for the Saudis to experience the American culture even for an hour in our restaurant*'.

#### ***5.4.2 Advertising and Communications***

The majority of the respondents agreed that advertising is not an issue for the international franchisors. Most of these companies have a local advertising agency that usually coordinates with the parent company when it comes to approving the ads or modifying the content. For example, respondent #4a stated, '*We have our private local company for advertising and promotion. We did not find it difficult to advertise our product*'. This respondent argued that their company did not find it difficult to promote their brand because Saudis travel well and are well educated and that some of the locals knew about the brand before it entered the Saudi market. Respondent #5 reiterated these comments and added that social media has also helped in promoting their brands.



The use of a local advertising agent was common. A local agency was used by respondent #2 to avoid paying the marketing fees to the franchisor, and their company rejected visuals portraying alcohol or women. When a local team is involved, as mentioned by respondent # 6, the advertising material must be authorised by the parent company. For example, respondent #7b commented that *'our company received feedback from the parent company to edit the advertisement language by using the most appropriate words to deliver the right message to the final customer'*. Local agents applied local knowledge, with respondent #8 stating that their company has an advertising agent in charge of evaluating the ads of the parent company to assess if it is socially acceptable or needs amendments to be suit the Saudi culture. For example, there was an American originated campaign celebrating the 45<sup>th</sup> anniversary of the business, but this ad was rejected due to inappropriate content, such as showing women's skin.

Respondent # 9a indicated that they have a marketing team that undertakes promotions in coordination with the parent company. Their company is inspired by the concept of their international brand to celebrate Saudi National Day. Therefore, a member of their marketing staff used the brand concept with its managerial hierarchy as a way of fun. The company applied this concept to the local market with the slogan, *'Come celebrate the Saudi National Day and Independence Day'*, and this advertisement was published in the local newspapers. They received a call from the Ministry of Interior regarding to the statement *'Independence Day'*, which caused an embarrassment for the company; however, the Ministry was understanding. In another case, respondent #10b mentioned that their company has a marketing team that communicates with the marketing department of the parent company and may make some modifications as per the requests of the parent company. However, this process is two-way: they added the Arabic language to the product packaging, and the parent company started using this language for its products.

Respondent #17 stated that they have a local marketing company that is approved by the franchisor. They do not pay marketing fees and use social media, such as Twitter, Instagram and marketing installations. In some cases, a dual system may apply, as illustrated by respondent #13a who claims that for local advertising, they have a Saudi company to deal with; however, regarding international advertising, there is a company in the Gulf region that is authorised by the parent company who they pay a monthly marketing fee.

Few companies rely on their own marketing department for advertising without the intervention of the parent company. Respondent #15 argued that their company has the ability, experience and knowledge of the country's culture, and the companies they deal with are very knowledgeable about Saudi customs and traditions. In addition, respondent #18a claimed their company relies on the word of mouth for advertising. Finally, as in any market, bad publicity can be dangerous. Respondent #11 recounted how there were Saudi tourists in Malaysia who were dining in a shopping mall food court and spotted a mouse in the restaurant. This incident was recorded on camera, and rumours spread that this had happened in Saudi Arabia.

Based on the findings, the culture of Saudi Arabia appears not to be a major issue for the international franchisor. The international franchisors are familiar with the Saudi culture through their visit to the country. International companies have managed to adapt to their marketing mix, product and promotion to fit the Saudi culture. Advertising appeared not to be an issue for international companies involved in restaurants, since a majority of the local companies have a local advertising agency that coordinates with the parent company for ad approval. However, adaptation requires the both franchisee and franchisor adding cost to its manual operation and procedure and require sufficient investments.

## **5.5 Legal and Regulatory Environment**

The majority of respondents agreed that that there is no franchise law in Saudi Arabia and the international franchisors experienced a real issue when dealing with country regulations due to the absence of a franchise law. For example, respondent 2 stated, '*The franchising regulations and legislation is not clear in Saudi Arabia*'.

Moreover, respondent #13b argued that there is no specific franchise law in Saudi Arabia because of the bureaucracy of the government, the desire of many businessmen to not have a specific franchise law and the absence of a Saudi franchise committee. There is a lack of people who specialise in both Saudi and international franchising laws according to respondent #20.

Respondent #11 commented that while the franchising law in Saudi was still unclear, there are attempts from the ministry of commerce to improve it. For example, the respondent argued, '*As a*

*franchisee, I have to register the brand name in the chamber of commerce as a commercial agency’.*

In contrast, others argued that the franchise law of Saudi Arabia is clear, and they do not have any issues with the country’s judicial system. For example, a participant of company #1 claimed, *‘The franchise laws are clear in Saudi Arabia compared to twenty years ago in terms of brand protection and the resolution of financial disagreements’.* This respondent argued that the religious and social aspects of a country takes time to change, especially in a conservative country and claimed that the added bureaucracy was not a problem for their company. Respondent # 3 argued that the franchising law is clear in Saudi Arabia because of the transparency and honesty of the Saudi juridical system.

There was common agreement that the regional and internal regulations hinder the franchisees from running their business smoothly. For example, respondent #19 stated, *‘What hinders the work of the franchisee affects the franchisors business. Internal country regulations, such as the availability of labour, the availability of electricity and the lack of work permits from the municipality, prevented us from opening the numbers of restaurants that had been stated in the contract’.* This respondent indicated that the company received warning letters from the parent company, which affected their relationship.

Respondent # 13b claimed that a change in supplier because of a ban from the Food and Drug Authority for meat from certain countries posed a challenge to their franchisor and affected the quality of their brand. The meat was obtained from Canada on one occasion and once from New Zealand and Australia. This affects the quality of the product and the taste for the customer according to the respondent. Chefs are trained using a specific type of meat so sometimes they end up serving raw bloody steak to the customer. Respondent #3, their company signed a twenty-five-year contract because of the difficulty and complexity of renewing a contract through the Ministry of Commerce.

### ***5.5.1 Arbitration and Intellectual Property Rights***

Most respondents claimed that an arbitration should be in the home country of the franchisors or in a neutral country. Respondent #15 argued that the reason for arbitration outside of Saudi Arabia is because of the franchisors' choice as they are familiar with the franchising law of their own country, which follows international standards, but also due to their ignorance of the Saudi law. Respondents #11 claimed that their parent company insisted that the arbitration was to be in the United States because of the lack of clarity regarding the franchise system in the Chambers of Commerce in Saudi Arabia. Moreover, Respondent #19 agreed to this because of the lack of clarity in the regulations of Saudi Arabia. Respondent #22a claimed that the arbitration of their company was in the 'neutral' Cayman Islands. Although Respondent #24 noted that the franchising laws keep improving, international franchisors follow their country's laws to protect themselves. However, Respondent #29 pointed out that '*Arbitration is not mutually satisfactory*'.

A few local companies claimed that their arbitration was going to be in Saudi Arabia. For example, the arbitration of few respondents such as #9a was in Saudi Arabia because of their familiarity with Saudi law, further, there was no resistance from the franchisor and Respondent #20 stated that the arbitration for all their brands was in Saudi Arabia.

Due to the lack of clarity in Saudi law, some of the respondents believed that the intellectual property of the franchisors was vulnerable. They stated that some international franchisors are concerned about their brands being copied by the master franchisees which is clearly stated in the contract. For instance, Respondent # 9b claimed that some international companies prevented them from sharing technological information with local companies to avoid copyright infringement to protect their intellectual property. Additionally, Respondent #2 also claimed that some local restaurants used a similar name for their brands for which the Chambers of Commerce took too long to investigate. Respondent #13a argued that many local Saudi companies, such as Kudo, are not in favour of granting sub-franchises to other local Saudis because the local franchisors do not trust the system. This respondent mentioned that there is no system to protect both the rights of the franchisor and the franchisee.

Respondent #9a claimed that their company used to grant sub-franchises of one of its brands to the local entrepreneurs – they had about ten sub-franchises but once the contract expired, they

opened their own stores and copied their business and their menu. Therefore, the parent company stopped granting more sub-franchises to protect its brand's intellectual property.

Moreover, Respondent #9b stated that '*When we granted the right to master franchise the fashion brands which similar to each other, the franchisors were concerned about the safety of its brands*'. This respondent claimed that both brands sell similar womenswear products so, their company assured both the franchisors that they would treat them differently. Further, this company has a brand of English pancakes regarding which, the franchisor had requested them to not have a similar brand. However, they still own another brand which serves similar products.

### **5.5.2 Saudi Customs Procedures**

Majority of the respondents believed that Saudi customs procedures might hinder the smooth running of their businesses. Moreover, Respondent #3 stated '*There are problems with Saudi customs such as the delay of the items that due to the port congestion and the malfunction of the crane*'.

For example, Respondent #9a mentioned that their company was waiting to receive a dough shipment from Turkey but unfortunately, the items expired because of the delays caused by the bureaucracy in the Saudi customs. The franchisor did not take responsibility for postponed or delayed loads. Many respondents cited examples of delays at both the ports and the airports – for example, the sauces arriving on a vacation day or paperwork needed for the permission to release the goods.

Respondents #16, indicated that their company experienced damage or breakage to their containers. Respondent #18b claimed one of their lobster containers was rotten due to the customs' bureaucracy and their company had to deal with the problem financially. Respondent #20 claimed that their company received broken goods or containers were missing. Respondent #13a claimed there was also a delay in opening one branch because the equipment was not received on time from Saudi customs. This respondent claimed that these problems also occurred in their fashion business – their company was supposed to get 134 containers, but they only received 132 containers. This respondent stated that one of the customs officers did not allow any female mannequins to be released so they asked the parent company not to send mannequins

with heads to avoid any problem that might arise. This respondent also mentioned that the fees charged for leaving the shipment for too long without release were increasing.

Despite these examples, some respondents claimed that they did not have an issue with the Saudi customs procedures. For example, Respondent #22a stated *‘the Saudi Customs regulations are not an issue as long as you adhere to the rules and we well prepared ahead of time’*.

Respondent #25 claimed that the Saudi customs staff were cooperative and once called them to check if one of their company loads was not given to someone else by mistake. Respondent #6 claimed they waited for three months to receive their goods, but this happened because of their company’s ignorance of importing regulations in Saudi Arabia, and Respondent #7b mentioned that their company hired a local company to deal with the Saudi customs procedures.

### ***5.5.3 The Regional Municipal Authorities***

Majority of the respondents agreed that they struggled with the lack of cooperation from the regional municipal authorities. For example, Respondent #18a stated *‘The municipality is seen as a challenge to the franchisee when some of its employees have a lack of information in terms of operating new businesses’*.

Respondent #19 provided an example of the ignorance of the municipality officials about business needs and methods: lasagne needs a day to ferment, but the municipal employee asked them why they did not get rid of the lasagne. This respondent claimed there is a lack of coordination among the local departments of the government. Respondent #26 claimed there is a lack of communication between the municipality and the private sector, and this ignorance impacts some of the decisions made for their staff. Generally, as Respondent # 19 stated, *‘The franchisor does not deal with these things and therefore the franchisor requires in the contract that dealing with country regulations is the franchisee mission’*.

Respondent #5 shared that one of their international restaurants has a kitchen design which is a standard design across the world but it conflicts with the local law in Saudi Arabia; hence, it had to be changed. In Saudi Arabia, the municipal regulations vary across areas and neighbourhoods. For example, in the Almalaz area, the municipality requested the company to follow rules that

were different from the municipality in Riyadh. The respondent claimed that their company found it difficult to explain this to the franchisor who had developed global business processes and systems.

Variations in municipalities pose a challenge not only because of a lack of clarity but also because of perceived violations of the law as the inspectors come up with new problems (Respondent #9a). Respondent #16 argued that the regional municipalities have operational systems which differ across cities, and the practices of different municipalities had confused their company when they were opening franchises in different cities across Saudi Arabia.

However, respondents #6 argued that the regional municipal staff are cooperative and provide them with feedback related to washing dishes and the quantity of meat that was supposed to be in the fridge. Respondent #7b claimed that they have no issue with regional municipal officials, they just check product expiry dates. For example, Respondent #24 claimed their company got a health warning about the tuna in their Jeddah chain, and their company dealt with it without having to go back to the parent company.

#### **5.5.4 Ministry of Labour**

There is a common agreement that employment poses a challenge in hiring well-qualified staff; Respondent #13 claimed *'I have noticed many companies started to focus on retail sector because, it is less headache compared to restaurants sector and does not require them to hire a lot of workers and dealing with some of government organizations'*.

Respondent #2 gave an example of how their company can't gain a restaurant license until 90% of the work is completed and the name of the owner is placed in the kitchen; so, paying rent for potentially two years before the labour is confirmed is too expensive. Moreover, the respondent mentioned that some of the employees can't even see their families for a long time because of the high fees of exit and return requested by the Ministry of Labour. Respondent #24 commented *'In the year of 2014, we could not open the planned number of stores due to lack of having employees so we sent the parent company an official letter to inform them and they understood it'*.

Respondent #26 also stated that their company struggled with the Ministry of Labour for employment and the expansion of their business. Respondent #30a stated that in one of their local brand restaurants, they tried to hire a female cashier in the Families section but it was rejected by the Ministry of Labour. Respondent #21c claimed that their company was planning to add a business line which involves a prepared pizza similar to the Subway service. The respondent argued this kind of business would run better if run by a woman, like their stores in Dubai, but the ministry of labour law in Saudi Arabia did not allow it and Respondent # 2 stated *‘The current franchisor of our brand is a woman and it is hard for her to get a visa without the attendance of a relative male guardian’*.

Finally, Respondent #30a indicated that in one of their branches, they wanted to employ twelve employees, but they only got four to five employees. This respondent felt there is discrimination from the Ministry of Labour, as some companies have enough staff whereas other companies do not.

Some of the interviewees consider the Saudization program is an issue in managing and operating their business activities. Respondent #20 argued the Ministry of Labour is not providing them with enough visas to hire expatriate staff because of Saudization. Additionally, Respondent #6 also indicated that the lack of visas and suitably qualified workers poses a threat to their business. It is hard to find Saudi chefs or waiters willing to do the job, and according to respondent #18a the lack of visas and high fees from the Ministry of Labour prevents them from hiring highly-skilled staff and consequently from opening more restaurants. Due to the Saudization program, respondent #31a claimed their company intends to employ more Saudis in order to obtain more visas to hire expatriates. However, Respondent #7b claimed their company tried to recruit Saudis to work at their stores by making announcements in their branches but no one came. Respondent #9a claimed that the Ministry of Labour comes up with new policies every time regarding to saudization. Respondent #22a argued that it is too expensive to hire Saudis as compared to other nationalities such Philippines, and it is also difficult to retain Saudis after training them.



### ***5.5.5 Real Estate and Property***

Most respondents agreed that renting property is difficult and can affect the company's business development plan and lead to the shutdown of the business. For example, respondent #3 claimed there is a problem with renting property to open new restaurants because of the landlords raising prices and not providing long-term contracts, and respondent #18a also stated that the rents are high and there is a lack of cooperation from the landlord. Moreover, Respondent #13a mentioned that their company was supposed to open three restaurants instead of one but the landlord asked them to leave the building, and the company did not have enough fiscal liquidity to open more restaurants.

Respondent #19 argued that international franchisors prefer a franchisee who is a real estate developer to overcome the problems related to property. This respondent argued that some landlords may increase the fees once the contract expires or may sell the property. However, respondents #17 claimed that renting and finding property is not an issue for their company.

It can be derived from these findings that the clarity of laws and regulations of the country is an issue for the international franchisor. For example, there is no franchise law to regulate the relationship between the franchisee and the franchisor. The franchise agreement is subjected as commercial agency. Therefore, the franchisor's intellectual property is at risk since there is no franchise law in the Kingdom, and the lack of lawyers who specialised in franchising field. There is no franchise association which can provide the franchisor with accurate information and advice. Many international franchisors prefer the arbitration to be in their home countries to avoid any problems that might occur with franchisee. Additionally, internal regulations, such as the Ministry of Labour, the regional municipality, etc, which pose a challenge for both the franchisee and the franchisors. This occurs because of the bureaucracy procedures and the lack of cooperation between the government officials and the private sector.

## 5.6 The Relationship between the Franchisor and Franchisee

All respondents agreed that the international franchisors preferred the master franchise<sup>11</sup> strategy to enter the Saudi market. For example, Respondent #25 claimed that their company signed a master franchise arrangement with international franchisors because the franchisor possessed limited knowledge regarding the domestic market related to the culture, religion, regulations and dealing with government bodies and the hiring of Saudis. Respondent #5 stated that *'we signed a master franchise strategy with the parent company so that we would have the right to be the master franchises in the Middle East and North Africa and also to have the right to give sub franchises'*. For example, this respondent noted that for one of their international brands, their company master franchises in the Middle East, but when it comes to Saudi Arabia, their company have only been granted the rights within specific territories including Riyadh and the Eastern Province while the rest of Saudi Arabia is operated by another franchisee. Respondent #2 argued that their company signed a master franchise agreement with the parent company because their company does not buy shares in the parent company because of the type of products the company offers, such as alcohol and pork. A different configuration was evident in the case of Respondent #3 who claimed that their company signed a master franchise agreement to grant sub-franchisees yet, the franchisee also owned shares in the parent company. Respondent #13a claimed that their company used to be an area developer, but the parent company changed a couple of terms in the contract and now they master franchisee in Saudi Arabia.

The exception to this general position was Respondent #22a who expressed a very different point of view. This respondent stated that *'The former master franchisee bought a 25% stake from the original company'*. The respondent claimed that the former master franchisee was inclined to buy stakes from companies that were on the verge of bankruptcy. However, the respondent also mentioned that former master franchisee claimed this decision to be one of the two mistakes he had made in his financial life in a recently published book.

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<sup>11</sup> This study found that Saudi companies signed master franchise strategies with international franchisors. The researcher used 'master franchisee' however, the researcher may also use 'franchisee' in another paragraphs instead of master franchisee.

### 5.6.1 The Royalty fees

Majority of the respondents refused to disclose how much their firms pay in royalty fees to parent companies. Respondent #24 stated *'The common challenge face by the two parties are the process of negotiation that related to the price of the brand , the royalty fees and the franchisee needs to get support at the beginning stage and after that things will be a piece of cake'*.

Respondent #9b claimed that the percentage of royalty fees they paid to the international franchisor varies. This company has the right to master franchise multiple international brands. For example, their company operated several brands in the restaurant sector and the royalty fees varied from 5% to 6% across brands. This respondent indicated that this percentage was based on the ratio and cost of the sales of the brand. For instance, Company #13a paid an initial fee of US\$ 300,000 for the brand and US\$ 50,000 for opening a new branch. The franchisee of Company #3 paid US\$ 1 million for the initial fees, plus US\$ 20,000 for opening a new branch and US\$ 10,000 fees for opening a small booth.

The respondents claimed that royalty fees could be paid weekly, monthly or every quarter. For example, Respondent #2 stated that their company pays 4.5% royalty fees every three months from the total sales to the franchisor; the company of Respondent #24 paid between 5% to 7% royalty fees to the franchisor and does not pay marketing fees, whereas Company #26 paid 12.5% to their parent company, with 4.5% deducted from the 12.5% which is given to the company for advertising.

Royalty fees may increase after the initial contract has ended and a renewal is negotiated. For example, Respondent #21c claimed their company signed a twenty-year contract to master franchise their brand and when the company signed another contract for a second term, the respondent expected the franchisor to increase the royalty fees. Respondent #13b claimed that the franchisor increased the marketing fees because there was a promotion campaign for the Middle Eastern countries so the company had to pay 5% royalty fees.

Some of the respondents expressed their concern regarding the inability to pay the royalty fees. According to Respondent #9a: *'There is a recent study from Alahli capital which indicates that the retail and restaurants sector will impact by 68% due to the bad condition of Saudi economy'*. Despite the economic pressures, this respondent argued that there is not flexibility from the

franchisors. For example, if their company is late in paying royalty fees, the shipments are delayed, and the franchisors do not care about the market conditions, especially German and Turkish franchisors. Respondent #13b stated *'our company sent letter to the parent company both in the retail and restaurants sector looking to reduce royalty fees and sent letter to the owner of the shopping mall'*. Respondent #13a claimed that one of the area developers of their brand had a problem with regard to low profits and mismanagement due to which they did not pay the royalty fees requested by their parent company.

Additionally, Respondent #22a stated that *'The former master franchisee refused to communicate with the parent company and won't deal with the team'*. Consequently, they have not paid royalty fees to the parent company since 2007. This respondent claimed that the contract was signed between the former master franchisee and the original company, and his company has nothing to do with it. However, the respondent indicated that their company does not mind paying a reasonable amount to their franchisor to settle the case and continue working together to enhance the performance of their business. They conducted a meeting with the Middle East chief operator in 2010–2012, and the parent company asked him to pay the previous US\$300,000 royalty fees to continue the business, but he rejected the deal.

However, some of these companies did not have an issue paying the royalty on time and were not impacted by the current economic hardship. For example, Respondent #1, an American restaurant, stated *'We pay the royalties on time as you know, we have the largest investment in the parent company so we own the business and the parent company own the name'*.

### ***5.6.2 Business Development Plan***

Some of the respondents mentioned that the international franchisor defined the criteria for their business development plan based on the size of the country and the population density. However, Respondent #13a, #17 added that plans were also based on the individual income per capita and consumer behaviour, and Respondent #20 added consumer demands and the diversity of the society to this list.

Majority of the franchise companies agreed that they couldn't meet the deadlines stated in the parent company's business development plan, which might hinder the success of the business

and the relationship between the franchisee and the franchisor. For instance, Respondent # 2 stated that *'The cost of establishing a new Japanese restaurant is very expensive setting the teppanyaki table with a vent is costly compared to opening fast food chains'*. This delay may occur for different reasons. These reasons are as discussed further.

#### ***5.6.2.1 Economic Conditions***

Some of the respondents claimed that the current economic conditions in Saudi Arabia, austerity measures taken by the government are affecting their business plans. For example, the respondent from Company #15 stated that *'the franchisor had asked us to open ten branches over the next ten years but the number was reduced to seven and the same happened for the other brand we operate'*.

Similarly, Respondent # 10a claimed that as a result of the economic conditions, their company was not able to open the required number of stores as agreed upon in the contract. It stated that the company had to open 20 stores within the following five years, but the company had asked the parent company to reduce the number to ten. In addition, Respondent #31a claimed their company was planning to open ten shops by the end of this year, but they could not because of the austerity measures which affected purchasing power. Respondent #3 noted that the salary reductions imposed by the Saudi government had a negative impact on the sales and contributed to the closure of the stores.

Respondent # 9a indicated that their company asked the franchisors to delay the opening of new stores for six months to study the market situation in Saudi Arabia. The company was expected to open ten stores but they only managed to open seven stores. They notified the parent company that they would try to open the remaining three stores in the following year. Moreover, Respondent #13a mentioned that the economic situation in Saudi also affected their sales and the company's inability to get rid of goods in one of its retail stores. For instance, Respondent #9c indicated that in their retail fashion sector, they could not open more stores for their brands because of low sales. Accordingly, the company tried to reduce the price, but this request was rejected by the parent company. Respondent #19 claimed that some shops were closed because

of a lack of profit. However, the Respondent #13b claimed that the American franchisor was understanding regarding the situation, unlike other European franchisors.

Along with the individual stores that some of the respondents considered, the delay in opening the shopping malls hindered their business development plan. For example, Respondent #9b claimed that there were also delays in opening new branches due to delays in the opening of shopping malls. Respondent #26 argued that there are some shops which have been relocated from the shopping malls to the public street due to lacking profitability and bad management of the shopping mall. However, Respondent #21d stated that their company is planning to close the stores on the street and focus on openings outlets in shopping malls. The street shops were not making profits, and there was little repeat business that the existing stores in shopping malls.

#### ***5.6.2.2 Infrastructure***

Some of the interviewees considered that the infrastructure of the country posed a challenge to open the number of stores requested by the parent company. Respondent #19 stated that *“Street closures and the length of maintenance prompted the closure of some our shops, and limited liquidity and the inability to find the right locations for new outlet”*. Respondent #14 claimed that their company also closed four shops because of the building of the metro and the associated excavations which caused a decline in sales. Respondent #26 claimed that four branches were closed due to the suspension of ownership to accomplish the project of the Saudi Metro, and one shop closed because of a terrorist bombing in the past. However, respondent #17 claimed that their company does not encounter problems because of the infrastructure of the country.

Some of the interviewees mentioned that difficulty in finding the right locations and choosing the wrong locations caused them to shut down their stores which hindered their business expansion. For example, respondents #3 and #19 argued that they had to shut down their stores because of the wrong locations. Furthermore, Respondent #7a claimed that there is a delay from the franchisee company in opening the number of stores stated in the contract. Respondent #7b mentioned that their company closed two shops because of the wrong location.

### 5.6.2.3 Competition

Majority of the companies believed that the presence of international franchises increased competition between local and international brands, which limited their market share. For example, Respondent # 6 noted that: *‘There is a competition between our international brands and the local brands such as Piatto and Steak House restaurant’*.

Respondent #1 claimed that it is difficult for international brands to enter the Saudi market as there is a lot of competition. For example, this respondent claimed that the local products owners better comprehend the country’s culture and its local people, whereas international franchisors focus on the location, number of units, implementation of the system, technology and the execution of their work. For example, Respondent #10b stated *‘Look for example to KFC when they trying to add rice to the menu to meet the needs of the Saudi customer, it took them to long to decide to avoid any mistakes that might affect the quality of their businesses, unlike the local brand Kudu's experience due to their familiarity with the Saudi culture’*.

Respondent #27 reported about the competition between their brand and local restaurants, such as Maestro Pizza, with reference to price, quality and market share. This respondent added that *‘The government austerity made the consumer to pay more attention to the price’*. Respondent #10b argued that due to high competition in the market, it is difficult for their company to find prime locations. Respondent #21a argued that local brands are supported by Saudi customers over the international ones. For example, Respondent # 6 argued that the local brand Albaik restaurant competes with KFC, and many Saudis prefer to support the local product rather than the foreign ones. Respondent #9b claimed the competition between the local brands and international brands is fierce. This respondent mentioned that many local brands copy their business so their company conduct studies every three years to understand their competitors’ new branches and promotions.

Moreover, Respondent #10b insisted that the increased number of international restaurants led to a reduction in the market share which affects their business development plan. Respondent #13a stated *“There is a delay from our company in paying the royalty fees for five or ten days due to the tough competition from other international brands that filled the market such as Five Guys which limits our market share”*. However, the respondent 13b argued that competition is a

healthy phenomenon, and a Shake Shack restaurant opening next to their brand would be a positive thing. If customers found that the Shake Shack is packed, they would come to the respondent's brand and learn about their restaurant. Moreover, respondent #10b mentioned that owning too many international restaurants in Saudi Arabia puts pressure on their company to open many branches, which increases the operational cost and reduces market share. Few respondents argued that local brands can't compete with international brands. For example, Respondent #18a stated that their company is not afraid of the competition because they have a new concept and there is a lack of high-end fine dining restaurants in Saudi Arabia. This respondent claimed that their brands are sophisticated and difficult to imitate. Moreover, Respondent #2 stated '*There is no local restaurants who compete with our brand due to the difference in what we offer and the high cost of setting up the businesses.*' This respondent claimed that opening a restaurant similar to his/her brand would be expensive because of the cost of importing the equipment and raw materials.

Alternatively, some companies argued that they had never been late in meeting the parent company's business development plan. For instance, Respondent #5 stated that '*Within five years we have to open 40 stores, so in our business development plant we made 11 stores per year instead of opening 10 stores per year*'. In addition, respondents #11 and #17 mentioned that their companies had never experienced any store closures or even faced a delay in opening new ones.

The researcher found that companies #28 and #3 are the only companies that had no conditions placed upon them regarding meeting the parent company's business development plan. Respondent #28 claimed that their company was not in favour of following restrictive rules in the contract as it might lead to frustration between the two parties. However, this respondent expressed concern regarding their economic situation.

### ***5.6.3 Training and Support***

Training is apparently an important factor for the success of the relationship between the franchisor and the master franchisee. Majority of the respondents reported that they are satisfied with the training they received from the parent company: '*We are satisfied with training, but there is always a need for training and to provide new items to the menu*' (Respondent #4a).



Respondent #11 proposed that the parent company equip them with the means for success by providing training programs to offer workshops and training courses outside the Kingdom. Respondent #5 stated that *'The parent company provided us with accredited programs which allowed our company to train new staff and then examined and approved through the parent company'*. The companies of respondent #7b had a training centre which allowed them to train new staff by a person who had been trained by the parent company. Their company received a training manual so that the parent company staff did not need to attend new stores to train them. Another approach illustrated by Respondent #1 was that the company sent the Head of Operations and their executive to the United States and their responsibility was to follow the parent company's systems and train their new staff. However, this respondent claimed that their company has a better training system than the parent company because of the cultural differences.

Respondent #17 stated *'We were satisfied with the training we received from the franchisors and we are entitled to train our new staff. The parent company sent us the materials and is running online live workshops'*. Training can, however, vary from one franchisor to another, even within a company that operates multiple international brands. For example, Respondent #1 stated *'Training is varied from franchisor to another as you know some of them have more sophisticated brands which believe in the continuity of education and training'* This respondent claimed that the American franchisor spent time with them throughout the company's business development, while other franchisors, such as a South African franchisor, focussed on the technical issues. There is a regional office for the American restaurant in Dubai which is accessible to their company for support and training, and the parent company has an e-learning system which allows them to watch the parent company's kitchen and staff live. Respondent #6 also indicated that they were satisfied with the training and support they received from all their franchisors. The American franchisors provided them with more support and training than the British franchisor. For example, a training program that fits with the host country's culture, for instance, closing shops during prayer time.

According to Respondent #25, the Americans are keen on training. For example, on the grand opening day of their restaurant, a team from the parent company visited to train them for two weeks, one month and sometimes for three months. Although their company had 400 outlets,

they did not ask the original company to come each time because over time, their company built the confidence to take care of the business. However, the parent company representatives frequently visited Saudi Arabia. Respondent #9b argued that the English franchisors are more flexible and cooperative in terms of assistance and cooperation, whereas the Americans, although they gave them a good product and provided their company with training at the start, they left and simply sold the name and the reputation of the brand.

However, few respondents argued that there is a lack of training and support from the franchisor. For instance, Respondent #2 stated '*The franchisor had no expertise and does not provide training to the franchisee*'. Similarly, respondents #3 argued that there is not enough training provided from the original company. This Respondent claimed that the parent company faced a dilemma in its operational management which prevented them from providing good training. Respondent #22a stated '*I have not seen the franchisor from 2007–2010 and have not receive any training*'. A financial dispute between the franchisor and franchisee caused their company to struggle with training and have a bad operational management system. Respondent #26 claimed there was insufficient training support from the parent company, especially when it came to marketing and advertising than the training at Burger King, McDonald's and Little Caesar Pizza. According to the respondent, the franchisor only looks for profit.

The continuity of training is an issue raised by several respondents. Respondent #14 indicated that the parent company generally provided training in the beginning but after that, no longer bothered to provide training and support. Respondent #18a claimed they do not have enough training and support, but they have well-trained staff from the franchisor. This respondent argued that the franchisor company trained them in the beginning phase and now they are in charge of training their staff. Moreover, Respondent #13a stated '*There is not enough support and training from the franchisor when it comes to operational matters and providing or adding new products to the menu in the restaurant sector but in the fashion chain we received a good training program with online training for our employees and the performance of our staff is evaluated by the parent company and the results sent to us*'. This respondent argued that It is expensive for their company to host the parent company representatives.

#### ***5.6.4 Franchisee Experience***

The fact that finding an experienced franchisee is a challenge for the international franchisor was unanimously agreed upon. This is the result of their poor management and the lack of financial resources to operate the business. Respondent #3 stated '*The Franchisor might face a problem to find a franchisee with a good experience on the restaurant sector*'.

Respondent #26 signed a contract with the American parent company in 1991. Between 1991 and 2011, their company had difficulty opening more outlets in the Saudi market due to their lack of management skills and not studying the market very well. Respondent #21a claimed that their company used to have 55 outlets but the number has reduced to 40, with closures because of internal managerial and financial problems at the franchisee company. This respondent argued that their company did not have enough expertise, unlike their partners in the UAE and Oman.

Respondent #26 claimed that their company had a bad experience with one of its sub-franchisees, and the company terminated the contract due to the sub-franchisees' lack of experience, inability to follow instructions about cleanliness and maintenance of quality. Their company offered to buy the outlet from the sub-franchisee and transfer ownership from the old sub-franchisee to a new one. Respondent #13a had a similar experience; they claimed that the area developer of one of their international brands in the eastern province of Saudi Arabia had undertaken service and price manipulation which damaged the reputation of the brand. The area developer did not adhere to the price and quality standards of the parent company, so customers ended up with a different taste and price each time he/she visited the restaurant or any other in the chain. The area developer was warned via letters from the parent company, and the parent company did not provide support. The area developer of this province had nothing to do with their company (because he had signed a contract directly with the parent company), and their sales were affected by the bad management.

A similar experience was found in Company #5 where the respondent claimed that one of the area developers of their international brand had financial problems and difficulty in managing the business. Their company offered to buy the outlets but the area developer refused to follow. Respondent #14 claimed that there are international brands, such as Wendy's, that have left the Saudi market because of the weaknesses in the franchisee management. This respondent pointed

out that Dairy Queen entered the Saudi market 40 years ago and left due to the lack of experience of the franchisee and was currently back as a result of a change in the company and its franchisee.

Respondent #19 mentioned that the two previous companies that used to master franchise their international brand failed due to mismanagement and the lack of experience of the franchisee. Additionally, this respondent gave an example of one of the famous Saudi company that operated international restaurants but lost a lot of international brands, including Taco Bell and Wendy's, because their company invested in real estate and construction and lost their concentration towards the restaurant business.

Moreover, Respondent #28 claimed that this is also illustrated by Starbucks which used to be managed by a local company but due to inexperience, the parent company suspended the contract and dealt with another local company. Respondent #27 insisted that there were good brands in Saudi Arabia, such as Smoky Burger and Elevation Burger, but they had failed due to mismanagement and the lack of experience of the franchisee and the unavailability of a good study of the Saudi market to determine the success of the brand and develop a clear plan. Finally, Respondent #3 claimed that the lack of the experience of the British parent company prevented them from expanding their business. This respondent further claimed that the original company had an issue in its management and operation system.

Furthermore, the Respondent #14 claimed that some of Saudi businessmen are ignorant about the benefits of franchising by saying '*You know American companies invaded the world through franchising*'.

### **5.6.5 Control Issues**

Majority of the local companies mentioned that some of the international franchisors placed strict conditions and terms in the contract which required franchisees to follow the parent company business regulations which controlled them and limited their freedom. For instance, Respondent #2 stated '*It was compulsory for me to import all the stoves and refrigerators from Beirut at a high cost*'. This respondent claimed that because of his Saudi nationality, the

franchisor believed they had a lot of money, and the respondent had come across other Kuwaiti franchisees who have faced the same problem with their parent companies. Additionally, Respondent #9a stated *'Turkish franchisors have also forced our company to purchase equipment from the parent company's homeland, even though getting the same equipment from the local market would make it much easier to undertake maintenance'*.

Respondent #14 claimed that the master franchisee of Wendy's restaurant was importuning unnecessary materials from the original company. The company used to import napkins instead of sourcing them from the local market, so the cost of importing was unnecessarily high, and the company had limited income which led to the failure of this brand. The company #10a was forced to import chapatti bread from the United States. Once, the franchisee company was running out of chapatti bread because of high demand so they found an alternative local source of supply without notifying the parent company. Consequently, they received a warning letter from the parent company. Following this, they discussed the sourcing of materials from the local market with the parent company, but the parent company disappointed them by stating concerns over the quality or the use of wrong methods of preparation. In contrast, Respondent #19 argued that importing the sauces and cheese from America was better than sourcing them from the local Saudi market, as the establishment of a local factory is expensive and also there is a need for warehouses to store the raw materials.

Furthermore, innovation outside the brand system is not always welcome. Respondent #10a claimed that their company is experienced in running restaurants, so they may come up with creative ideas that they would like to implement. For instance, Respondent #10b claimed that the parent company is not flexible when it comes to adding new varieties of dishes during Ramadan, such as dates and soup, which may increase sales.

The majority of respondents agreed that the parent company does not need to visit to oversee the selection of a new location. For example, Respondent #18a stated *'When it comes to choose new location, we send information and pictures of the location, the franchisor does not need to attend'*, and Respondent #2 added *'For opening new shops, Karaoke sent to the franchisor and approved by the franchisor'*. Respondent #28 claimed that the parent company relied on the experience of the Saudi partner because of their familiarity with the region, and there is a

scoreboard that the parent company used which endorsed decisions based on a voting system. In addition, Respondent #4a claimed that the parent company did not engage in selecting new locations – their company had to inform them. There is, however, a variation in practice. Respondent # 9a argued that regarding the choosing the locations, the Turks, Germans and British intervene, whereas the Americans and Thais did not because they believed that their company had built a trustworthy relationship with them over time.

However, there are some common disagreements between the partners. Respondent #20 indicated that *‘There is a difference of views between our company and the parent company’*. An example for this was a debate over which city is more profitable for a new restaurant – Jeddah City or Riyadh, the Saudi capital. There was a disagreement regarding the determination of the price of the product and a proposal to remove some items from the menu. For example, Respondent #3 argued that some cookies are not in demand, but the franchisor insisted on including them in the product range. This Respondent claimed the franchisor intervened in determining the brand price which was supposed to be similar to the price of other the Gulf States. Respondent #6 mentioned that their company follows a system to determine the price with reference to their prices in America. Respondents #6 stated *‘The British and American franchisors are involved in the process of hiring key people such as the operations manager and the franchisors might request to interview them’*. However, respondent #3 claimed that the franchisor does not interfere in the recruitment process and hiring the key positions.

Some companies claimed that the extent of control varied from one company to another and from one brand to another and relied on the franchisor’s ability to control the business from home. Respondent #11 commented that *‘The relationship between the franchisor and the franchisee supposed to be good’* and argued that if a disagreement occurred between the two parties due to a lack of consistency from the franchisee to follow the terms of the contract, the franchisor would take action and apply for arbitration, typically in America. Although it was likely that the franchisor would win the case, it would be difficult for the franchisor to manage 200 outlets in Saudi Arabia and other stores in the Middle East without the franchisees’ support. Consequently, the franchisor should have a very good relationship with the franchisee because the franchisee is in a strong position. In this case, the respondent claimed that there is a

difference of views between the both parties, but it did not reach the point of seeking termination of the contract or going to arbitration.

Respondent #25 stated that *'I think it is an equal relationship between the franchisee and the franchisor'*. The reputation, financial position and the status of the company often gives the franchisee company the right to set some conditions in the contract. For example, Company #24 claimed that they succeeded in convincing the parent company to reveal their recipes. The respondent insisted that the UAE and Kuwait were forced to import sandwich bread from America, but the parent company could not force them because their company has many branches in the Kingdom with around thirty-two chains, plus five sub-franchise chains.

Respondent #4a argued that the franchisee had control over the franchisor because ultimately, the business is in located in Saudi Arabia.

Some of the franchisee companies had claimed that they suspended their contracts with the parent company for different reasons. For instance, Respondent #13b stated that *'We used to have a French coffee shop and we did not continue the contract with the parent company'*. This respondent claimed that the brand was not famous enough and hence, this venture was not profitable. Moreover, as a result of the presence of Dunkin Donuts in the Saudi market which was selling their products at inexpensive prices, the company asked the parent company to end their contract after running the business for three years. It was a friendly settlement, and the brand still exists in France and other European countries.

However, control does not always rest with the franchisors. Respondent #12 mentioned that their company used to have a contract with a Lebanese brand, but they did not renew the contract with them. The contract ran for six years, and the respondent did not know the reason for ending the contract. Respondent #9a claimed that they signed a contract with almost 13–15 international brands worldwide. They have a year-long program called 'Incubation' to test the global brands and their applicability in the local market. If the brand is accepted, it will be transferred to the next stage which called the 'Segment' which identifies if the brand belongs to either restaurants or food beverage. This respondent argued that if the brand is not successful in its first year in the local market, they have the right to suspend the contract. There are conditions in the contract regarding this matter, and the franchisors have no problem with it. For example, they terminated the contract with one of their international brand although the American restaurant brand still

exists in other countries such as Dubai and Bahrain. This respondent argued that running the business for seven years is enough.

Finally, Respondent #14 postulated that many Saudi franchisees do not pay much attention to the contract terms because they fear that the franchisor might change his mind if they add too many conditions to the contract. This respondent claimed that this is in favour of the franchisor and is thus an unjustifiable fear. The franchisor requires the franchisee to consult a lawyer before signing the contract, and after signing the contract, the franchisee has more power than the franchisor.

Respondent #26 insisted that the relationship between the parties is not a partnership system – it is all about paying and selling the product. Respondent #28 indicated that the Saudi company has more control over the business than the franchisor, owing to their ability to act quickly and their ability to make decisions because of the absence of the franchisor. Respondent #17 claimed that in his previous working experience, he knew a big brand name company that had made concessions to enter the Saudi market.

### **5.6.6 Monitoring**

All respondents except one agreed that the franchisors visited their companies to monitor the business at least once a year, and they never experienced an issue with their franchisors. *‘The British franchisor visits us two to three times year while the Americans visit us four times a year for inspection and monitoring the business’* (Respondent #6). Respondent #16 also reported that the franchisor visited their company two to three times a year, and mystery shoppers are employed by parent company to monitor the business. In the case of Respondent #24, the parent company has a representative office in Singapore which is in charge of monitoring their restaurants in the Middle Eastern countries, and Respondent #26 claimed that their parent company has a regional office in Lebanon, and the representatives visit them five to ten times a year with a coordinated visit to their branches. The company operations team’s directors and managers monitor its business around Saudi Arabia. Internal monitoring is also conducted. According to Respondent #10a, their company has as monitoring program called ‘Model



Capability'. In this program, the operations manager visits its branches every 45 days, and the District Manager and Manager of their restaurants make weekly visits.

Respondent # 9a reported that *'The Turkish franchisors visit us each month due to the increase of the stores number'*. Their company received feedback after the visit stating that the number of employees in the restaurant was not enough, and they made suggestions about the product temperature. Feedback for Respondent #15 was about the service, the method of serving the dish – with the clock fingers and serving to children first and then to women and men. There were also some notes about the continuity of monthly cleaning and not keeping the meat with the pre-cooked chicken.

Some of the franchisee companies claimed that some of the stores make more profit than others either because of their location – open in shopping malls – which leads to increased number of employees in these stores. For example, Respondent #10b stated that *'If one of our restaurants experience low number of repeat customers, we do not neglect the service or serve bad quality food, but we might reduce the number of the employees'*.

According to Respondent #11, some stores make more profits because of the high number of repeat customers but that does not let them neglect the ones that do not make as much money, as this will affect their business standards and product quality. An inventory of some of their outlets which was conducted with their franchisor enhanced their company's credibility and transparency with the franchisor. Respondent #17 claimed that their company sent a weekly report although the parent company never bothered asking why some stores are more profitable than others. Respondent #7a claimed that their companies communicate with the parent company through email and Skype, financial information is exchanged monthly and the franchisors do not interfere in the sales percentage of the stores, while the respondent # 9c hold a weekly meeting through Skype or over the telephone.

However, few companies are either not satisfied by the monitoring process that is undertaken by the parent company representatives or have never been monitored by the parent company. Respondent #7b stated *'We are in charge of monitoring the business through our operations manager, the British franchisors never pay us visit'*, and Respondent #19 stated that they did not share a close relationship with their parent company. The respondent claimed that the presence

of the parent company office in Dubai to monitor their restaurants has poor performance and mismanagement which causes damage to their business. Respondent #13b argued that the franchisor has difficulty in following up on the quality of the product, the non-compliance of the franchisee within the terms of the contract, the lack of success of the work and the laxness of the franchisee to follow up and to monitor the business, especially if there are many parties in the contract.

All the respondents except one claimed that they did not receive any incentive or reward from the international franchisor for monitoring the business while the franchisor is away. For example, respondents #2 claimed their companies do not receive any reward to maintain the business standards and quality. This Respondent claimed that only profit is important to the franchisor.

The exception to this position was Respondent #31a who mentioned there are incentives from the Saudi parent company (Master Franchisor). For example, their outlets received first place in terms of quality in Riyadh which gave their company the priority for initial expansion and having the prime locations.

The behaviours of the restaurants managers is a monitoring issue. Some of respondents agreed that the restaurant managers are not following the business standard and there is financial theft done by restaurant manager. For example, Respondent #31a claimed that their company offered incentives based on the restaurant's financial performance. However, this respondent also commented that sometimes the staff complained about the overtime working hours. This respondent added the following: *'We have laid off two managers due not following the company regulations after giving them a warning for a couple of times'*.

Respondent #4a mentioned that their company offered rewards, such as a monthly increase and a letter of appreciation, to the restaurant managers. However, this respondent also admitted that they had laid off managers due to financial theft and a failure to follow company regulations. Respondent #19 noted that their company gave random incentives based on the profit made by the shops but not permanently. This respondent stated that *'Our Company also experienced financial theft from the restaurant managers'*. Respondent #13a added that there had been instances of theft by staff from the customer by switching bills between different groups who

were dining in the restaurant. However, Respondent #9b argued that there was camera surveillance in their restaurants for monitoring to avoid financial embezzlement. Other controls, according to Respondent #15, include good accounting systems and a strong financial control department.

Sharing information with the franchisor was seen as monitoring issue by some respondents. Cultural attitudes according to Respondent #14, underpinned the problem of disclosure of financial information by the franchisee to the franchisor. However, this respondent insisted that things have changed slightly because of corporate governance. Additionally, Respondent # 4b *'There is a challenge for the franchisor in terms of finding experienced franchisees who are willing to share information with franchisor'*. Moreover, Respondent # 4b stated *'The problem in Saudi Arabia is that Saudis do not trust each other in terms of exchanging information'*. In fact, the issue with sharing of the information is mutual. Respondent #13a stated that the international franchisor benefits from a lack of clarity in the franchise law in Saudi Arabia because the franchisor is not obliged to disclose financial information to the franchisee, unlike in the United States. The willingness to share financial information is based on their ability to monitor and control performance.

Based on these findings, there are issues that might impede the relationship between the franchisee and the franchisor. For example, paying the royalty fees on time is a challenge for the master franchisee. There are some cases where the master franchisees were not be able to pay the royalty fees for different reasons such as the economic condition and the lack of profitability. The inability of some franchisees to meet the franchisor business development plan, the economic condition and the austerity measures taken by the Saudi government caused the customer to become more price-conscious. The country's infrastructure, such as street closure, caused difficulty in finding the right location. There is strong competition among the local restaurants and even among the international restaurants which limits business development plan. Training does not seem to be an issue as the franchisors provide training manuals and live workshops online, some the master franchisees have a training program and, sometimes, send one of their staff abroad to be trained by the parent company and then take charge of training their company staff.

Additionally, the lack of experience and the difficulty in finding well-experienced local partners with financial capability pose a threat to the success of international brands. The franchisor asserts control over the master franchisee by forcing the master franchisee to import the raw materials, determine the price and the intervention in the hiring process which affects the relationship between both the parties.

The process of monitoring the franchise business appears an issue. Monitoring the behaviour of restaurants managers appears an issue such as not following the company business standard and rules and there are a couple of financial thefts that have been reported by the franchisee. The master franchisee and the franchisor face an issue regarding the sharing of information because of the conservative nature of society and the absence of franchise law which obligates both parties to disclose the information.

## **5.7 The Summary**

This chapter has presented the findings from the field study, which included the analysis of qualitative data from 31 companies generated using semi-structured interviews with directors, general managers, chief executive officers and operations managers. Five themes emerged from the analysis of the interview data: the role of franchising in developing SMEs, the influence of religious considerations, the influence of cultural considerations, legal and regulatory environment and the relationship between the franchisee and the franchisor. These findings provide a picture that demonstrated the importance of international franchises to the development of SMEs in Saudi Arabia. From these findings, it can be concluded that international franchises are considered a means of growth of small and medium enterprises in the restaurant sector. The international franchising had a positive role on encouraging Saudi SME owners to start their own brands and improving their managerial skills and to be innovative in developing their business. International franchises did not help in providing jobs for the locals in Saudi Arabia. Religion and culture did not hinder the international franchisor's entry into the Saudi market. The law and the regulations of the country are identified as an obstacle that may affect the franchisor's decision to invest in this country. Finally, some issues were identified which may affect the relationship between the franchisee and the franchisor such as paying royalty fees, business

development plan, , the experience of the franchisee, control and the issue of monitoring and a symmetry of information. The next chapter will relate the findings to existing literature.

## **Chapter 6: Discussion and Conclusion**

### **6.1 Introduction**

The findings of the research presented in the previous chapter will now be discussed by relating them to existing literature and other studies, and to the stated objectives of this research. This will provide clear and rich information on how international franchises contribute to the development of Saudi Arabia. This chapter will be examined under three headings relating to the objectives of the theses. First, the role international franchises in three areas: supporting SMEs and entrepreneurs; enhancement of managerial skills; transfer of technology and the provision of employment. Second, the obstacles that may impede the operations of international franchising in Saudi Arabia and finally, the applicability of agency theory to the Saudi context will also be looked into.

### **6.2 The Role of international franchises in emerging economies**

These areas emerge from the findings.

#### **6.2.1 Supporting SMEs and Saudi Entrepreneurs**

The resource scarcity theory (Castrogiovanni et al., 2006; Keating, 1989; Sanghavi, 1998) suggests that international franchising helps small and medium enterprises (SMEs) to grow and rapidly expand. The respondents in this research agreed that international franchises help the Saudi SMEs to grow for two reasons. First, the low risk that is associated with international franchising, compared to running traditional, independent small businesses. This is supported by (Boe et al., 1987; Peterson and Dan, 1990), who claim that people choose to become franchisees because international franchisors have tested and well-established business model names, when compared to running a high-risk, new business. Within the context of Saudi Arabia, this is supported by (Sadi and Henderson, 2011; Sadi et al., 2011). Sadi and Al-Fuzai (2010) claimed that there is a relationship between international franchising and SMEs. International franchising assists SMEs in Saudi Arabia to expand because they might confront some difficulties and restraints at the initial stages. Rezvani and Hajifathali (2013) also claimed that international

franchising had a positive and important impact on the growth of SMEs in the Iranian food industry. The findings of this study support

Second, international franchises support local SMEs through outsourcing raw materials such as products with short expiration dates from the local market. Holt (2003) stated that international franchising reduces capital flight by giving the opportunity to invest in the host market.

Respondent #1 agreed with this: *'Many of small and medium enterprises owners see us as a reformer and coach, and we helped them to grow the company which will lead to recruit more people, and we helped them to raise the awareness of having a high-quality product. Our vegetables are locally sourced'*

Alharbi (2014) stated that international franchising has contributed to various sectors in Saudi Arabia, with about 4% of it in services such as transportation, recreation, rental cars and real estate. A study by Fath (2007) also found that international franchising played an important role in developing SMEs in Egypt. The author claimed that the food sector was quickly improving; initially, every ingredient was imported, but after a couple of years, young Egyptian businessmen started developing food factories certified by global brands. As a result, factories became competent in making quality goods, meeting the local demands, following which these businessmen started exporting their goods abroad, throughout the Middle East and Europe. Many global investors invested in Egypt's contemporary slaughter facilities. Small factories improved to provide uniforms for restaurants and reduce the high importation fees. However, there are still financial, technological and legal barriers that confront SMEs in Saudi Arabia, preventing them from fully benefiting from international franchises, as noted by (Alharbi, 2014; Merdah and Sadi, 2011; Otsuki, 2002).

An important conclusion derived from this finding is that a strong relationship exists between international franchises and the growth of SMES in Saudi Arabia. The international franchise has a well-established business model that limits the risk of starting new businesses and increases the rate of success and business productivity.

Regarding the role of international franchises in encouraging young entrepreneurs to start their businesses, the findings of this study are in a line with what other academics claim in the literature (Alon and Banai, 2000; Knot, 2003). The respondents of this study agreed that

international franchising helped local entrepreneurs expand and run their business within the country by providing a good distribution-supply network. They also enhanced their vision and helped transfer the experience and knowledge of SMEs franchise companies to local entrepreneurs. Respondent #19 stated *'Approximately 80% of the Saudi entrepreneurs benefited from international franchises in the development of management skills and the process of trade exchange and I was one of these people who benefited'*.

This was also noted by (Caves and Murphy, 1976; Lafontaine, 1992; Rubin, 1978) who stated that franchising is an structural model chosen by entrepreneurs in the services field where a distributed system of chains is needed to attain competitive advantage. This is supported by (Ali, 2008; Kayed and Hassan, 2011; and Sadi and Henderson, 2011;) who claimed that Saudi entrepreneurs found international franchising to be an essential tool in overcoming the problems they had encountered such as marketing and leadership skills . Franchising already has a concept, a plan and a high level of success in its home market, thus a reduced level of risk. Sanghavi (2001) notes that local entrepreneurs in the developing market benefited from the franchising brand name and its well-known reputation and develop their local brands through imitation of the business model.

However, despite these positive impacts, it was found in this study that many international franchisors granted master franchises to major Saudi companies with huge financial resources, limiting chances for Saudi entrepreneurs to benefit from the business model.

### **6.2.2 Technology transfer and innovation**

Price, Stanworth and Purdy (2001) stated that international franchising helps in transferring technology, through a “learning organization” and improvements in staff performance and capability, in terms of areas such as hardware and machinery learning. However, the findings of this study are not consistent what the literature suggested about international franchises helping transfer technology to the emerging market (e.g. Fath, 2007; Knott, 2003; Sadi and Henderson, 2011)

The respondents of this study claimed that international franchising did not help in transferring technology to the Saudi restaurant sector. The fact that the restaurant sector does not require



advanced technology, and due to its availability in the market, some of the master franchisees have advanced systems, as compared to the franchisor. Respondent #13b argued that *‘our company follows a global system Aloha that is used globally by franchise companies’*

Teegan (2000) argued that many of the positions in franchising do not transfer or develop skills in the local market. If one considers improvement in the abilities of a local cook in a McDonald’s restaurant, for instance, it is difficult to identify the “transfer of know-how.” However, there may be, considerable support extended to the economy and culture, if those with few commercial skills learn how to cook, serve customers, earn a living, run a retailing operation, work in a team, and avoid crime and the underground economy. In addition, the transfer of technology and know-how by the franchisor should be seen more holistically, at a country level, and not simply from the vantage point of a particular job.

Nour (2015) identified the different channels of technology transfer in the Arab countries, focusing on Sudan and the United Arab Emirates. The author covered several sectors such as manufacturing, metal, food industries, chemicals and textiles, paying attention to the company size. However, none of these sectors used master franchising strategy as a way of transferring technology. This suggests that international franchising is not directly associated with technology transfer but varies in terms of sectors and franchisors. A study conducted by the Chamber of Commerce (2005) focused on consumer services and restaurants, accounting for 74% of the total activities operated by franchise system, claimed that international franchises did not transfer technology in these business activities.

Tuncalp (1991) stated that franchising strategies in Saudi Arabia is based on some form of trading activity, such as importation, marketing, or distribution, between the franchisor and franchisee. However, if the franchise business can be seen to lead to a transfer of technology, then a joint venture strategy can be structured which would provide a number of benefits to the franchise partners – tax holidays, access to public funding, and duty-free imports. In addition, At-Twaijri (1989) stated that the laws mandate transfer of technology as requirements for forming a joint venture in Saudi Arabia (A Guide to Establishing Joint Ventures in Saudi Arabia, 1985). Alon and Alami (2010) stated that Moroccan entrepreneurs with financial resources are more interested in forming joint ventures with American partners as a way of licensing technology and modernising their facilities.

Elsaman (2017) mentioned that franchising is different from technology transfer agreements. A technology transfer agreement is a type of licensing agreement where a license is provided to the transferee to start a manufacturing entity to produce a product utilising the transferor's technology, without having control over the way the licensee runs its business. In contrast, a franchise agreement is only a restricted license that permits the franchisee to utilise the franchisor's trade name or mark to deliver their products or services; the franchisor has unlimited control over the franchisee's way of running of the business. Licensing is therefore a way of transferring technology, as compared to franchising where there are restrictions placed on the franchisees. Merdah and Sadi (2011) claimed that Saudi SME owners prefer to involve themselves in licensing strategies for technology transfer with their foreign partners.

However, the respondents of this study agreed that international franchising had a positive business impact on the master franchisees. Rubin (1978) mentioned the experience of franchisors assisting the franchisee to be more creative and innovative to start its own individual business activities. The respondents of this research agreed that international franchising stimulated SME owners to be creative and create their own brand concepts. Respondent #17 stated *'Based on our previous experience of managing international brands, we came up with our own concept'*.

However, with the increase in the number of local brands, these local franchisors became rivals to the international ones. This is also noted by Ali (2008) who stated that Saudi entrepreneurs developed more than 30 local concepts within the Saudi market and some of these concepts travelled abroad. These SME companies helped other local companies design menus and provide support through business incubators. Lewin (1999) claimed that research and development are the franchisor's main assets in the field of innovations.

The overall conclusion that can be derived from this study is that international franchises have a positive impact through the enhancement of innovative thinking and creativity among Saudi Arabian SME owners, who in turn create their own brands and become franchisors. But there is limited impact in terms of direct technology transfer and this is may vary from one sector or strategy to another.

### 6.2.3 Managerial skills

The findings of this study are in line with what other academics have claimed in the literature (Michael, 2014; Peterson and Dan, 1990; Stuart and Brownmen, 2001) noted that international franchising transferred well-established and tested business models and know-how to host markets through the improvement of managerial skills and providing training.

The respondents in this study agreed that international franchising helped SME owners improve and enhance their managerial skills and capabilities by providing them with good training and workshops and advice on how to manage their budgets and financial resources. International franchising is seen as an educational instrument, teaching the business owners how to acquire and train staff and how to communicate effectively with the staff, the suppliers and the distributors. Respondent #10a claimed that '*International franchising taught our company on how to manage workers' movement in the kitchen and the distribution of the machines such as setting up the warehouse, cooling and the number of workers needed in the restaurants*'.

Oxenfeldt and Kelly (1969) who stated that franchising is a good choice because of the franchisee's need for a ready supply of management labour and skills enhancement. This is noted by Sadi and Henderson (2011) who claimed that international franchises in Saudi Arabia assisted the franchisee in improving their managerial skills by following well-established businesses in terms of providing good training and hiring staff policy. The SME owners benefited from the franchisor's distribution networks and supply chain management skills by embracing their financial system, such as the ability to make decisions, saving on recruiting, providing good training, having good inventory systems, and adopting different styles of management. The significance of acquiring a franchise is the benefit of training and receiving competence skill (Choo and Bowley, 2007; Khan, 2016; Price, 1993). Fath,(2007) noted that many local Egyptian marketing and advertising companies were creative with their ads, impressing the citizens with good advertisements via national TV and creating a different practice of thinking for the workplace and customers, such as in terms of bonuses and coupons. The packaging of products was improved with artistic designs, utilising more competent and high-quality items to fulfil the needs of the dealers and suppliers.

An important conclusion from this study is that international franchises is a means for SMEs owners to enhance their managerial skills and the transfer of expertise among SME owners in Saudi Arabia. Particularly, franchisors with big brand names who have possessed managerial skills, efficient supplies and suppliers providing labour.

#### **6.2.4 Employment Creation**

The findings of this study are not consistent with what the literature (Alon and Welsh, 2001; Preble and Hoffman, 1995; Welsh and Alon, 2001) who claimed that it can contribute to economic growth through employment generation. The respondents of this research agreed that it did not directly help in providing jobs in the Saudi restaurant sector. This is contradictory to (Ali, 2008; Chanut et al., 2013; Elsaman, 2017; Sadi and Al-Fuzai, 2010; Tuncalp, 1991) suggest about the positive impact of international franchising in providing jobs to the **emerging** market.

This is attributed to cultural reasons such as the societal outlook towards working in restaurants, which contributed negatively and turned Saudis away. This is supported and noted by others (Al-Kibis et al., 2007; Hartvigson and Hourani, 2009; Rowings et al., 1986; Yadav, 2005). Bell (2005) stated that Saudis are not interested in working in restaurants which affects the international franchisors' ability to recruit Saudis, because they are more driven by status and are not in favour of working in low class positions, such as restaurants. Ramady (2010) also noted that Saudis are less willing to do physical work and social status is extremely essential for the young generation, with this influencing social relationships and marriage. For example, Respondent #3 stated *'We found it difficult to recruit Saudis because of the nature of the work such as baking and cleaning the kitchen'*.

Leonidou (1991) stated that most companies working in Saudi Arabia rarely recruit national citizens for their sales position because personal selling, in these regions, is seen as a low-esteem position. Recruits are from neighbouring Arab countries such as Palestine, Egypt and Sudan.

Despite, the incentives and rewards offered by companies, The Saudization percentage is very low which indicated that there is high turnover in this sector. Respondent # 9a stated *'We tried to*

*keep the Saudis through providing good training programs along with other incentives, for example, if the employee continues with the company for three years, he can get a car loan without interest, and if he continues for five years, he can obtain an administrative loan without interest, but the majority of them quit unless they feel forced to stay because of their financial situation.'*

Rice (2004) stated that one of the main issues in enforcing Saudization is the traditional Bedouin attitude that despises any kind of manual labour and positions related to it. This is so deeply rooted that even an engineer who works with machines and wishes to marry is seen somewhat inferior because of his position related to manual labour. Saudization adds to the costs for local companies and does not succeed in encouraging Saudis to work in low status jobs and it is hard to retain them (Abughazala, 2006; Gresh, 2000). Leonidou (1995) stated that salespeople are often encouraged and rewarded by offering commission on sales, cash rewards and sales contests in Saudi Arabia. The turnover rate of sales personnel in Saudi companies is high.

Previous studies claimed that the restaurant sector worldwide is confronted with high turnover. Fast food franchises have high turnover rates as they employ young staff who easily leave for another job (DiPietro, 2003). It has been mentioned that in the fast food sector the turnover rate of hourly and salaried workers was more than 150% annually (Ebbin, 1999). International franchising may succeed in terms of employment in different sectors such as banking, the hospitality and retail sector. For instance, according to a report published by the Mackenzie global institute (2015), the number of Saudis working in the retail sector doubled between 2010 and 2014. This is an area where Saudi women in particular have found employment; according to the Ministry of Labour, their numbers jumped from 10,000 in 2010 to 120,000 in 2014. This reflects a push by the government to encourage Saudization and the feminisation of retail categories catering to women, such as lingerie or cosmetics. This maybe because women have limited options for choosing a career. Most of the previous studies were based on the Saudi male perspectives since women were not allowed to work in restaurants. However, things have now changed following the Saudi government's lift of the ban on women driving and allowing them to work in restaurants. Kaikati (1979) stated that Saudi women are not permitted to engage in the workplace, all salespersons are men, even in shops selling exclusively ladies products. This could stimulate further studies to explore these changes.

One conclusion that can be derived from this study is that there is no direct relationship between international franchises and job generation in the restaurant sector in Saudi Arabia and this also varies from one country to another.

### **6.3 Obstacles that may impede the operations of international franchisors in Saudi Arabia:**

Three potential obstacles emerged from the findings: religion, culture, and legal considerations.

#### **6.3.1 Religion**

The transaction cost theory (Williamson, 1991) suggests that environmental uncertainty in the host markets raises the ex-ante and ex-post transaction costs, particularly due to information search and adaptation costs. The respondents in this study agreed that although gender segregation exists, it was not a major issue to the international franchisor. However, adaptation is very important to the norms and religious customs of the country.

The majority of international franchisors adapted their restaurant design which incorporate individual entrances, one for families and one for singles; this has cost implications. Harrison et al. (2000) who postulated that it is very essential for global firms to adapt to issues that are sensitive to the country's religion. In the Saudi context, several authors note the need to observe religious customs (Ali, 2008; Francesco and Gold, 2005; Sadi et al., 2011; Sadi and Al Fuzi, 2010; Sadi and Henderson, 2011). Tuncalp (1991) mentioned that the segregation of single women from men who are unrelated to them is a tradition that is strictly implemented in Saudi Arabia.

The majority of restaurants have partition walls or provide them based on the customer's desire for a family section. Respondent #20 stated *"When it comes to the wall partition in family section we do have 60% of our restaurants, where the families can dine in an open area and 40% of our restaurants, where the families can dine in private space."*

Tunsi (2000) stated that the Saudi customer's loyalty is impacted by the interior design of the restaurant. Saudis appreciated restaurants that offer private partitions, as they tend to seek privacy when eating out with family. Moreover, having a family and single section is not an

issue since some of these restaurants are designed for takeaway or collection or they are in food courts in shopping malls which does not require a singles or family section.

A conclusion of this study is that gender segregation and prayer time are not major issues for both the international franchisors and the master franchisee. The need for segregation and outlet closure are well known and accepted, but does more incur additional costs and adaptation to some procedures, such as increasing the number of the staff in family section. This requires sufficient investment by both, the franchisee and franchisor. This require the franchisee to have diversified portfolio which require sufficient investment when it comes the adaptation to the norm of the culture and religion otherwise this will lead inefficient bearing risk problem where the master franchisee expect compensating from franchisor if he does not make returns on investment.

The respondents of this study also agreed that closing restaurants during prayer time is not a major issue and does not affect their business operations and sales since all shops do the same. The majority of outlets are open for long hours daily so they will be able to compensate for lost sales during the time. Al-Zahrani and Hasan (2008) stated that the majority of fast food outlets stay open later and with longer hours in Saudi Arabia.

The international franchisor adapted their operational manual (operation hours for opening, training employees to deal with prayer time and adapting their cooking procedures) to suit the religious norms of the country. This is supported by Sadi (1994) who stated that adaptation is important to the operational polices of the host country. Religion is an essential influence that the global franchisor needs to consider once they chose to enter global market. Knowing the impact of religion is important because social norms have a great influence on human behaviour (Cialdini and Goldstein, 2004; Sunstein, 1996). Moreover, the customer is accustomed to the system and the rules of the country and some restaurants ask all consumers to leave the restaurant and stay outside during prayer time, whereas other premises permit the consumers to stay inside. For instance, respondent #11 stated *'The closure of stores during Prayer time, I have no problem as long as the other shops shut down and consumers are aware of the purpose.'*

The Saudis prefer shopping at night when the last prayer is over and it is cooler. The shopping activity usually reaches its peak level in the evening, particularly during weekends in Saudi

Arabia (Alawi 1986; Kaikati, 1976). Saudi Arabian families with children like to dine at restaurants during evenings due to the climate (Al-Othaimen et al., 2007). Closing restaurants appeared not to be a major issue. However, this requires additional cost to the operational management.

In contrast, it has been found that Ramadan is an obstacle for the international franchisor which contradicts the transaction cost theory. Higher environmental uncertainty, due to the franchisor's insufficient knowledge to assess the sociocultural, economic and institutional elements of different countries, means that they need to delegate responsibilities to the franchisee to reduce environmental uncertainty in host countries. The respondents claimed that international franchisors allowed them to add new dishes to the menus to meet consumer needs by adding local dishes. Contractor and Kundu (1998a) stated that an American restaurant franchisor delegated its Egyptian franchisees to offer a new dish during Ramadan. Despite the adaptation, Sales fell by more than 50% and more for the majority of international brands during the same time. Respondent #2 claimed that *'during Ramadan sales fell by 70% especially during the first two weeks of Ramadan, and then started to pick up a little bit during the last days of Ramadan when people were getting bored of the traditional cuisine.'*

This is because of the change in lifestyles of the Saudi people during the holy month. Deresky (2008) claimed that Saudis prefer eating traditional food at home during Ramadan. Business activities in general tend to slow down, with limited working hours in almost all sectors (Seyyed et al., 2005). Rice (2004) stated that in Ramadan, working hours are shortened and Saudis may be exhausted from night-time religious and social activities. Shujaiddin (2009) stated that during Ramadan, work hours are limited from eight to six hours and restaurants are shut down during the day and only open for business after sunset, except hotels. However, it has been found that in this study not all sectors were impacted negatively by the sales plunge in Ramadan. For example, the clothing sector and coffee shops sales increase due to the Eid festival. Ahmed (1999) stated that during Ramadan, sales of some items, such as dessert related to Ramadan and dates, increases. Respondent #9b stated that *'sales fell in Ramadan by 60% to 70% and this also varies from one restaurant to another. For example, sweet and pastry shops may not be as badly affected as other restaurants due to the Eid season.'*



This study conclude that Ramadan impede both the international franchisor and franchisee sometimes it is hard for the master franchisee to pay the royalty fees and recover the slowdown of their sales in the coming months. Mutual cultural understanding is very important to overcome this barrier.

### **6.3.2 Local Culture**

The findings in this study confirm what other scholars have claimed in the literature that adaption to local culture is crucial to reduce environmental uncertainty. (Castrogiovanni et al., 1993; Cox and Mason, 2007; Narver and Slater, 1990; Szulanski et al, 2003; Yin and Zajac, 2004). Fladmoe-Lindquist (1996) and Hodgetts and Luthans (2003) stated that global franchisors need to modify their standard businesses in order to succeed in the international market. The respondents of this research agreed that the culture raises some issues for the international franchisor. Alon and McKee (1999) claimed that the dissimilarity between cultures increases costs for international companies. However, the franchisors managed to adapt their brands to suit the consumer local culture in terms of preference, taste and level of cooking, portion size, etc. Elbashier and Nicholls (1983) stated that due to cultural differences between the British and Middle East, some of the British companies embarked on important product adaptations or developed new products for the Arab countries. Hoffman and Preble (2004) who stated that international franchisors need to pay attention to the tastes and habits of the national consumers as well as the price. For example, respondent #10b stated *'we excluded some dishes that had a low demand such as coconut ice cream and the fish sandwich and instead they added kufta sandwich with tahini.'*

The franchisors often received invitations from the franchisees to visit the country to familiarise themselves with the culture. In this study, it can be said that the product is the most curated element of the marketing mix, because of climatic conditions, unique topography, large households, high purchasing power, strict religious views, and varying consumption lifestyles (Elbashier and Nicholls, 1983; Kaikati, 1976; 1979; Leonidou, 1991; Tuncalp and Yavas, 1986; Yavas and Tuncalp, 1984; Yavas and Glauser, 1985). Leonidou (1991) stated that due to the size

of the country, the existence of a wide warehousing system and the presence of regional depots in the main, urban regions to source the closed areas, is essential. Hot temperatures require certain goods to be stored under cold storage conditions. Ocwieja (1975) noted the importance of adaptation and development of special protective packaging in Saudi Arabia due to the exposure to extremely high temperatures, and the difficulty of handling products during transport through massive deserts.

In addition, some of the respondent raised the issue of language to both the franchisee and the franchisor. Miller (1992; 1993), who claimed cultural uncertainty occurs due to the insufficient knowledge of other international cultural elements, such as language. The Chamber of Commerce in Saudi Arabia requires a copy of the franchise agreement written in Arabic to be registered. This requires the international franchisor to hire lawyers who are fluent in both Arabic and English. Some of the government officials do not speak English which causes complications. Hartvigson and Hourani (2009) who indicated that the language of Saudi Arabia was an issue to western franchisors.

Moreover, some of the international franchisors do not speak English so they hire a translator. However, there is a difficulty in transferring ideas and the translation may lead to misunderstandings. Respondent #29 stated *“As you know Koreans do not speak English They are proud of their language there is an English translator for the franchisor but there is difficulty in transferring the idea and there is a delay in responding to email.”*

Respondent #7b commented that *‘our company received feedback from the parent company to edit the advertisement language by using the most appropriate words to deliver the right message to the final customer.’*

Elbashier and Nicholls (1983) claimed that some international firms operating in the Middle East consider linguistic differences as an issue in their international marketing, especially in translating brand names and slogans. Al Agha (2009) stated that translators find it difficult in Saudi Arabia to translate the MacDonald’s menu into Arabic and might not have the ‘know how’ to phrase certain words or groups of words, so the translator leaves them in English due to culture-specific terms. For example, ‘Chicken nugget combo’ translated to ‘دجاج نقت’. The word ‘nugget’ is translated into Arabic ‘نقت’. Tuncalp (1991) mentioned that the Saudi franchisees

have complicated accounting considerations. The franchise needs to keep accounting records in Arabic and use the accounting systems in accordance with the country to meet the requirements of the Saudi government's Ministry of Commerce, and the Department of Zakat and Income Tax of the Ministry of Finance and National Economy. Furthermore, the franchisee needs to follow the accounting standards of the franchisor, maintaining records in English to meet the audit requirements of the franchisor. However, there is an issue regarding the process of the exchange rate to follow in the translation procedure, unless the franchisee hires accountants that are capable of maintaining accounting records, both in Arabic and English, and the franchisor employs independent accounting companies in Saudi Arabia that can conduct audits in both languages.

The language, particularly translation, barriers consume time and money, increasing costs and sometimes leads to a loss of interest in conducting business with other countries. The transaction cost may also be higher for translating materials such as the operations manuals, contracts and brochures. The conclusion is that language is an issue to the success of the business and may hinder the growth of prosperity of the relationship between the master franchisee and the franchisor.

### **6.3.3 Legal considerations**

Transaction cost theory (Williamson, 1975, 1985) environmental uncertainty impacts the contract structure as a governance system. It also prevents the franchisor from devising in-depth contract conditions and raises the need for ex-post modifications by providing decision rights. The findings in this study are in a line with what other authors (Briggs and Araghi, 2009; Chanut et al., 2013; Young, 2001) claimed that the absence of specific legislation, regulations and franchise laws in Arab counties, particularly in Saudi Arabia (Abughazala, 2006; Alharbi, 2014; Mikwar and Akkad, 2011; Taqi, 2007) are an obstacle for the international franchisor.

The respondents of this study also agreed that the absence of franchise laws is an issue for the franchisor. This is noted by Shujaiddin (2009) who stated that there is a need for amendments

because the franchising system is still unclear, and many global franchisors confront challenges to grant a franchise business to Saudi businessmen.

Tuncalp (1991) stated that there are no franchising laws in Saudi Arabia. For instance, if the franchise contract includes a clause requiring that the agreement will be managed by the laws of a different country, this requirement will not be implemented in Saudi Arabia. The Saudi courts will follow only the Sharia law for solving the disagreements between the franchisee and franchisor, no matter what the parties have decided upon in the contract. For example, a contractual agreement where the franchisor forces the franchisee to buy some of its supplies only through the franchisor may be prohibited in the United States, but this behaviour could be allowed in Saudi Arabia. The lack of an institutional infrastructure of the country impedes the development of franchising and may lead to asymmetry of information and the determination of the type of strategy the franchisor prefers to enter the market.

Cole (1992) stated that although Saudi Arabia used a secular system for commercial law, the Sharia law (required of the person in his relationship with Allah) is still common. For example, if a business deal leads to unjustified risk or profit (both not allowed by the Koran), its contract can be invalidated on this basis. In addition, civil codes can be modified without notification, and there is no prevention of retrospective legislation, unlike in the West. This suggests that the implementation of sharia law contradicts with the franchising international law which force many international franchise companies to do arbitration in their homeland

There is a lack of lawyers experienced in franchising field which impede the success of international franchising. Tuncalp (1991) stated that Saudi laws require the Saudi company that allocates money to a foreign company, which does not have an office there, to be accountable for charging tax from such payments. Therefore, the tax liability of the international franchisor for the initial franchise fee and the regular royalties has to be examined. This is an issue for international franchisors, unless they employ a lawyer who is familiar with Saudi law to represent its interests in Saudi Arabia.

In addition, the respondent agreed that the franchise agreement is registered under commercial agency laws. This is supported by Ali (2008), who stated that franchise agreements in Saudi Arabia are treated as commercial agency laws. For example, Respondent #11 stated that *'as a*

*franchisee, I have to register the brand name in the chamber of commerce as a commercial agency.'*

Alharbi (2014) argued that there are implications and complications in using commercial agency laws, such as different interpretation of rules and regulations of the franchising agreement among government departments, including the ministry of commerce, ministry of labour and other financial institutions. The majority of these government departments do not distinguish between franchisee and franchisor as they deal with the franchisee as a branch of the main company, even though it is an independent unit. Sometimes claims may be dismissed by courts because the franchise agreement is not well defined in commercial agency law.

In the absence of a franchise law, intellectual property appeared to be an issue for the international franchisor in this study. Doherty and Quinn (2000) who claimed that international franchisors use coercive power to protect their trademark from being misused. Within the context of Saudi Arabia, this view is also supported by Ahmad (2012) who mentioned the protection and application of intellectual property rights in Saudi is not strong and this is also an issue for the Gulf countries (Leonidou, 1991). In Saudi Arabia, for instance, the insufficient protection of patents and copyrights is an issue in the government system. International partners frequently advertise "cautionary notices" of their patent rights in national newspapers in order prepare for future claims to these rights in Saudi courts (A Guide to Establishing Joint Ventures in Saudi Arabia, 1985).

The lack of transparency of the legal system is an issue for the international franchisor in protecting their trademark and intellectual property in the restaurant sector. Maritz et al. (2007) stated that the protection of intellectual property rights is an issue due to the absence of laws, especially with regard to the protection of the uniforms of restaurant staff in Saudi Arabia. For example, Leonidou (1991) stated that piracy and replication is a common phenomenon in the Gulf States. For instance, there are counterfeit shampoos, disinfectants, window cleaning agents, travel goods, sports clothes etc. El Zeiny and Cliquet (2007) stated that one of the issues confronting international franchisors in Egypt is the protection of property rights, and Tyre (2013) also claimed that McDonald's harboured concerns over the weak protection of intellectual property in Egypt and Algeria due to the lack of the franchise legal system.

The respondents agreed that the bureaucracy of internal regulation, such as the Ministry of Labour, Saudi customs and the regional municipality are issues, for both the master franchisee and franchisor. Respondent #19 stated *'what hinders the work of the franchisee affects the franchisors business. Internal country regulations such as the availability of labour, the availability of electricity and the lack of work permits from the municipality prevented us from opening the numbers of restaurants that had been stated in the contract.'*

Respondent #3 stated *'There are problems with Saudi customs such as the delay of the items that due to the port congestion and the malfunction of the crane'.*

A study conducted by Chamber of Commerce (2005) found that the master franchisees claimed that they confronted obstacles in importing regulations, procedures and customs clearance. Dunn (1979) stated that bureaucracy can be difficult for American businessmen in the Gulf States. Vessels can stay in port for months before they are allowed to unload because of customs clearance. There is a difficulty in getting entry visas for visiting investors to follow the business. Visas are not automatically permitted in Gulf countries, particularly for multiple visits, and often need sponsorship by a local agent. Danish and Smith (2012) claimed that hiring specialist female's trainers from abroad is not allowed in Saudi Arabia because of the restrictions on issuing business visas for foreign females.

Respondent #2 stated *'The current franchisor of our brand is a woman and it is hard for her to get a visa without the attendance of a relative male guardian.'*

The findings of this study concluded that judicial rules and policies may also increase the transaction costs. In summary, whilst religion and the underlying Saudi culture have implications requiring some adaptations to products, policies and procedures, which result in additional costs, on the whole these issues are well known, and the need for adaptations has been established. Ramadan has considerable implications for sales performance, but this applies to all business in the sector. The protection of the franchisors' intellectual property rights, however, remains an area of major concern for many. The use of coercive power from the franchisor to protect its trade mark appeared an ineffective because Saudi Arabia follow sharia law and the enforcement of the contract is weak.

## **6.4 Applicability of Agency Theory in the Saudi Context**

This research explores the applicability of agency theory in the Saudi Arabian context. The relationship between franchisee and franchisor is important to the success of the franchise business. Agency theory has been used to examine this relationship in western countries (Combs et al., 2004; Brickly and Dark, 1987; Kidwell et al., 2007; Jensen and Meckling, 1976; Rubin, 1978; Eisenhardt, 1989a; Shane 1996a) particularly, within the context of the United States. Most of the previous studies examined agency theory from the perspective of a developed market perspective but in this study it is examined from the perspective of franchisees who are from a developing market, Saudi Arabia, and who are conducting business with international franchisors from a developed country. Franchise research has focused primarily on concern of franchisors (Dant, 2008) whereas this study focus on the franchisee perspective. This study focused on the Saudi Arabian context which is different from western countries at the legislation system, religious, cultural, economic and political level. The relationship between the franchisee and franchisor is pertinent in the following aspects commonly identified in agency theory: royalty fees and business development plans; training; franchisee's experience; control; monitoring and asymmetry of information.

### **6.4.1 Royalty fees and business development plans**

The findings of this study are in line with what others suggests in the agency theory (Combs et al., 2004) that franchisees can cause damage to the franchisor's business by failing to pay royalty fees and following business quality standards. The respondents agreed that paying royalty fees is an important issue. The condition of the Saudi economy, the fluctuation of oil prices (Meijer, 2010, Mensi et al, 2017; Raphaeli, 2005) and austerity measures have impacted the restaurant sector and the purchasing power has fallen. Ramady (2009) noted that the rising inflation that hit Saudi Arabia in 2006 affected the economy. It negatively impacted Saudi citizens, affecting their purchasing power. For instance ,respondent #13b stated that *'our company sent letter to the parent company both in the retail and restaurants sector looking to reduce royalty fees and sent letter to the owner of the shopping mall'*.

Leonidou (1991) stated that usually the transactions between the supplier and the wholesaler in the Gulf States are completed on a credit basis, usually delivered within 45–60 days. However, because of the liquidity problems in the Gulf economies, which became even more severe after the Gulf War, there was a need to expand credit periods. The liquidity problems are also experienced by customers who have started to purchase durable commodities on credit. A study conducted by the Chamber of Commerce (2005) showed that franchisors argued they do not receive royalty fees on time from their Saudi partner. Mseddi and Bouri (2010) noted that Tunisian franchisees failed to pay the royalties fees to a foreign franchisor of McDonald's and Pizza Hut, as a result these chains left the market. The economics of a country is an external factor that affects the business performance of the franchise.

Academics such (Blair and Kaserman, 1982; Rubin, 1978; 1990) argued that franchisors should lower royalty fees to encourage the franchisee to look after the business. If the brand-name reputation of the franchised business decreased, it will impact negatively on the franchisor income. This is very important to avoid Qusi-rent appropriation issue since it has been found in this study the master franchisee operated multi-unit which indicate that the franchisor has less power to use quasi-rent appropriation in international market such as Saudi Arabia. Economic uncertainty such as financial crisis increases the risk of business, transaction costs .Within this context, an important conclusion to be drawn from this study the issue of paying royalty fees that identified in the agency theory is an issue in the Saudi restaurant sector, meaning that the possibility of opportunistic behaviour, such as shirking a rise.

Moreover, it has been found in this study that opening the required numbers of outlets is an issue for the success of franchisor's business development plan. This is consistent with what several authors argue in relation to the agency theory (Mullner, Bernardi-Glantz and Schnedlitz, 2003), that the franchisee's capability for managing the business efficiently is the most important component in avoiding failure. This includes the ability to accomplish goals, the capability to cope with management issues and sufficient planning during the establishment of the business. There was a common agreement among the participants that their companies could not meet the franchisor's scheduled business development plan for various reasons. First, due to the current economic condition of Saudi Arabia, the fall of oil prices and austerity measures that effect purchasing power. Tuncalp (1991) stated that the franchisee for Dairy Queen was required by the



franchisor to expand through the Kingdom. Since 1981, the company has opened three outlets in Riyadh and one outlet each in Al Khobar, Dammam, Jeddah and Al Jubail for a total of seven outlets. The firm was planning to increase the number of its outlets into Taif and Madinah city with three additional outlets, but the recession in the Saudi economy compelled the company to postpone these growth plans.

The respondent from company #15 stated that *'The franchisor had asked us to open ten branches over the next ten years, but the number was reduced to seven and the same happened for the other brand we operate.'*

McCosker (1995) and Mendelsohn (1999) stated that external factors, such as currency devaluation, aggressive and inexpensive rivals, recession in the economy, government policies and diplomatic relationship between two countries, lead to franchisee failure beyond franchisee power. Studying and evaluating the target market is very important, such as doing SWOT analysis to avoid economic uncertainty. The master franchisor's local knowledge is very important in reducing the transaction costs and saving time.

Second, because of the lack of infrastructure and the logistic system of the country. Mustafa (2011) stated that Saudi Arabia is confronting supply chain and logistics challenges such as: labour issues, lack of logistics infrastructure, and supply chain staff skill levels. Respondents insisted that poor infrastructure impacted their business negatively, leading them to choose poor outlet locations. A bad location could also be the factor that leads to franchisee failure (Mullner, Bernardi-Glattz and Schnedlitz, 2003). Respondent #19 stated, *'Street closures and the length of maintenance prompted the closure of our shops, and limited liquidity and the inability to find the right locations for new outlet'*.

This point is supported by Harif et al. (2011) who claimed that the wrong locations led to franchisee failures in Malaysia. Tuncalp (1991) claimed that finding the right location affected the franchise development phase in Saudi Arabia. It is common to find franchises tucked away in hard to find side streets. Some of them are positioned on major avenues without parking lots. There is also one franchise that has put three outlets very close, within one square kilometre of each other. Another has an outlet on a major boulevard including a spacious parking lot, but the store sign is so small that one can only see it when very close to it. Eskander and Aal (2010)

stated that it was hard for IKEA's agent in Saudi Arabia to find a shopping mall that could rent out such a huge area for the company, and Alon and Alami (2010) mentioned that one of the reasons leading to the failure of Subway in Morocco was the difficulty of finding the right location at the right price. Choosing the wrong location may lead the master franchisee to free ride because the desire to generate quick returns of the investments, to supply lower quality products due to the lack of customers and cut cost. As a consequence, this leads to conflict between the franchisor and the master franchisee. The level of urbanisation and the improvement of transportation played an important role in the success of the businesses and in reducing costs by encouraging the international franchisor to invest in the country and prevent the capital flight.

Third, the respondents claimed that heightened competition between themselves and local restaurants (low cost operation, competitive advantage, local knowledge) limited their market share. This is supported by Maritz et al., 2007; and Swartz, 1997; Tuncalp, 1991, who stated that international franchises raise the level of competition in Saudi markets between the local and international brands. For example, respondent #10b stated *'Look for example to KFC when they trying to add rice to the menu to meet the needs of the Saudi customer, it took them to long to decide to avoid any mistakes that might affect the quality of their businesses Unlike the local brand Kudu's experience due to their familiarity with the Saudi culture.'*

Tough competition leads to other marketing issues and a price war between business owners. A study conducted by the Chamber of Commerce (2005) found that the franchisees claimed establishments in places where the same activities exist, resulting in price competition and harming the business in the long term. Abughazala (2006) claimed that franchisors started to shape new alliances, in the form of joint ventures with investment firms taking control of the operations in Saudi Arabia, to meet the tough competition in the Kingdom. Competition is an external factor that affects or limits the success of the business and may lead the master franchisee to free ride. The master franchisee benefited from the company well reputable brand by serving low quality product and manipulating price. Horizontal agency issues occurs when franchisees free ride on other outlets. This is because all outlets run under a same brand name (Brickley and Dark, 1987; Caves and Murphy, 1976). However, this may encourage local entrepreneurs to get involved in franchising as a competitive strategy vis-à-vis competitors

(Michael, 2014). This may also urge the franchisor to develop and improve its product and efficiency, thereby less competitors leave the market and provide the consumer with more options and improve their welfare.

Moreover, the respondents agreed that the Saudization program impacted negatively on their business development plan. The master franchisees are no longer able to hire labour from abroad, and hiring and training Saudis are costly, which limits their ability to open the required outlets. For instance, respondent #24 commented *‘In the year of 2014, we could not open the planned number of stores due to lack of having employees, so we sent the parent company an official letter to inform them and they understood it.’*

Abughazala (2006) stated that enforcing Saudization was a challenge in terms of providing staff calibre and this impacted business development. The supply of labour providing skilled workers, such as providing chefs, waiters, and employee retention can impede the business development plan. Furthermore, the researcher noted that opening casual dining, upscale restaurants and fine dining are costlier options than opening fast food restaurants, which may hinder the business plans and lead to a conflict between the two parties. Respondent #2 stated that *‘The cost of establishing a new Japanese restaurant is very expensive setting the teppanyaki table with a vent is costly compared to opening fast food chains.’*

This is supported by Tuncalp (1991), who stated that Saudi franchises of restaurants, such as the Carvery and the Sizzler Steak Houses, stayed as single outlet operations because of the more expensive nature of the services they offer. This is a required high investment, and the financial capability of the master franchisee is a foundational factor in overcoming this issue. **This also** requires sufficient investments by both master franchisee and franchisor. The length of the contract is also an important factor – signing a contract for ten or twenty years is better than five to allow the master franchisee to open the required restaurants and grant sub franchises.

The researcher also observed that the Saudi companies are the master franchisees and are not in favour of granting sub franchises for different reasons, which somehow limits the company’s ability to meet its business development plans. Respondent #10a claimed that *‘our company has been allowed to give sub franchises within a certain area, the west region of Saudi Arabia, but in*

*general the parent company is not a big fan of giving sub franchises because of the difficulty of controlling and maintain the quality of the business.'*

Tuncalp (1991) noted a common, potential issue of the master franchise strategy in Saudi Arabia. Many Saudi franchisees are hesitant to sub-franchise because of their tendency to maintain all the business for themselves and to eventually expand their franchise into a chain of wholly owned outlets controlling a large part of the Saudi market. However, if the initial franchise outlet fails to generate immediate profits, Saudi franchisees think twice before opening other outlets in different regions. Opportunism can take the shape of adverse selection, where franchisee initially overstate their capabilities to achieve a mission, such as opening the required outlets (Katz and Owen, 1992). The entry mode of this strategy impacts the business development stage. This suggests that even though the master franchise strategy is more suitable for countries with dissimilar cultures, it appears that this strategy has a weak side and impedes the franchisor's business plans.

The conclusion that can be drawn from this study is that meeting the franchisor's business development expansion is barrier for them. It is important for the international franchisor to fully evaluate the Saudi market before entering and seek the best person, with local knowledge, financial ability and good experience.

#### **6.4.2 Training**

The agency theory (Justis and Judd, 1989) suggests that the franchisor–franchisee relationship can be problematic if the franchisor does not provide proper training or support to the agent. The respondents of this study agreed that training was not an issue for the master franchise in Saudi Arabia. The franchisor provided them with training at the beginning and they also received training manuals and live workshops running online. In addition, some of these companies had training centres to provide training to the new staff. For example, respondent #17 stated that *'we were satisfied with the training we received from the franchisors and we are entitled to train our new staff. The parent company sent us the materials and is running online live workshops.'* In addition, respondent #5 stated that *"The parent company provided us with accredited programs*

*which allowed our company to train new staff and then examined and approved through the parent company.'*

Abdelgawwad (2012) stated that the Egyptian quick-service restaurant franchisees do not have an issue with the training and support received from the franchisor, and neither did the MacDonald's in Morocco, as reported by Alon and Alami (2010). This is because quick-service restaurants do not require high-skilled training. This also seems to be the case in Saudi Arabia. Quick-service restaurants do not require highly skilled or trained staff, whereas casual dining restaurants require highly qualified staff. The fast-food concept, with simple menus, quick product finishing, and service times, lends itself to the standardisation of products and service delivery systems, which are easy to franchise (Lashley and Morrison, 2000). In contrast, casual dining restaurant franchisors must dedicate significant attention to providing comprehensive training strategies, making a competitive service plan, and reforming current operational strategies to be successful in the global market where the customers' expectations are much more complicated (Lee, 2008).

In addition, the agency issues are different from sector to sector. For example, the service sector issue is different from the goods sector. Alharbi (2014) argued that the nature of the relationship between agents and manufacturer is different from the relationship between the master franchisee and the franchisor in Saudi Arabia. In the automobile sector, agents use commercial agencies, which are different from the master franchise strategy. For example, the manufacturers do not provide the Saudi agents with manual operation and do not have a standard business model

Overall, the findings of this study conclude that master franchisees are generally satisfied with the training they receive from the international franchisor and it is not an issue in their relationship. Providing good training reflects positively on the franchisee performance which limits the possibility of opportunism and free riding. This means that the training issue identified by the agency theory does not apply to Saudi Arabian context.

### 6.4.3 Franchisee Experience

The findings of this study are in line with other scholars (Elango, 2007; Kersi et al., 2013) who state that franchisors interested in entering the foreign market should have the skills to reduce possible opportunistic behaviour by the franchisees. The respondents of this research agreed that the lack of experience of the master franchisee is an issue for the international franchisor. Eisenhardt (1989a) stated that opportunism leads to moral hazard, where the agent makes less than the optimum effort to generate output on behalf of the franchisor. Abughazala (2006) stated that the careful selection of trustworthy, reputable franchisees is very important to protect against intellectual property infringements in Saudi Arabia.

Some of the companies have had little experience and knowledge in terms of managing a business with limited financial resources. For example, respondent #3 stated '*The franchisor might face a problem to find a franchisee with a good experience on the restaurant sector*'. This is supported by (Mullner, Bernardi Glattz and Schnedlitz, 2003; McCosker, 1995; Mendelsohn, 1999; Miranda, 1995) who stated that the franchisee capabilities and skills is important to the success of franchise business.

Academic scholars (Kaynak, 1984; Yeoh and Wong, 2011; Zoubir, 1999; Martin, 1999) stated that finding local representative with a good experience in the Gulf States is difficult. There is a dilemma and difficulty of changing the Gulf agent in the future (Leonidou, 1991). Yavas et al. (1994) argued that any international businessmen who isolate the current Saudi partner would find it difficult to start new partnerships and look for other chances due to the tiny and unified nature of the Saudi business society. This suggests experienced franchisees with sufficient knowledge about the local market is very important for the success of the franchise and limiting environmental uncertainty. Providing the master franchisees with incentives may solve the issue of adverse selection through encouraging them to do better. This also indicates the lack of personal and entrepreneurial skills of the Saudi franchisee in dealing with challenges in the local market is a challenge for the franchisor, which may drive away their desire to invest in the country and increase the monitoring cost.

In addition, the respondents agreed that some master franchisees are not actually familiar with the concept of “franchising”, despite the efforts of the ministry to educate the public. Lee (2008) mentioned that potential franchisees may not completely understand the nature of a franchise business since it might not be a common business format in certain countries.

This is supported by Tuncalp (1991) who claimed that the Council of Saudi Chamber of Commerce and Industry conducted seminars about franchising relations between the Saudi businessmen and with the commercial section of the American Embassy and a bunch of experts from the United Kingdom. The ignorance of Saudi businessmen regarding the importance of franchising negatively impacted its development in Saudi Arabia. Alharbi (2014) argued that the franchising concept is still not popularly adopted by the majority of domestic SMEs in Saudi Arabia. One of the reasons for the absence of franchise funds in Saudi financial institutions is the limited understanding of the franchising concept. El Zeiny and Cliquet (2007) stated that ignorance of the franchising concept was the first hurdle impeding its use in Egypt. However, the ignorance of the concept among Saudi businessmen may appeal to many international franchisors and franchise consultation companies because of the lack of competition from the domestic business owners.

The researcher also noted that the majority of interviewees in this study are not Saudi citizens, especially the operation managers, so their lack of knowledge of the Saudi culture and dealing with local consumers may contribute to the failure of business. Tuncalp (1991) stated that Saudi master franchisees delegate responsibilities to people, hired from neighbouring countries, who have no experience in running restaurants or are unfamiliar with the franchise business model, damaging the business. The business ethics and commitment of the master franchisee is essential for the success of the business. Having a partner-operated business line or company is better than running multiple brands and firms.

The conclusion that can be derived from this study is that finding an experienced master franchisee is important for the international franchisors as this reduces the risks of opportunism and moral hazard, which are identified in the agency theory.

#### 6.4.4 Control Issues

The findings of this study are consistent with other scholars (Ayling, 1987; Knight, 1984; Withane, 1991) who stated that franchisees are concerned about the restrictions placed on them, and their lack of ability to make a decision. The respondents of this research agreed that the international franchisor exercised control over the master franchise in terms of importing the raw materials. This is an issue for the master franchisee. For example, Respondent #9a indicated that *'Turkish franchisors have also forced our company to purchase equipment from the parent company's homeland, even though getting the same equipment from the local market would make it much easier to undertake maintenance.'*

This is supported by a study conducted by the Saudi Chamber of Commerce (2005) which claimed that the franchisor imposed on the franchisee certain of raw materials and requirements for production and capital equipment, despite the local existence of these materials at equal quality and competitive prices. This indicates that there is a possibility that international franchisor engagement in opportunistic behaviour. Dant and Nasr (1998) stated that the franchisor should recognise the franchisees' need for some independence. This is essential to motivate them to look after the business. Leonidou (1991) stated that in the past, the agent in the Gulf States had a rather submissive role in the marketing of the principle goods, now he plays a more active role and is more demanding (e.g. wants to have punctual deliveries, more advertising support, better prices, etc.). The master franchisee's need further autonomy to be more creative and innovative. Such disagreement increase due to uneducated, untrained, and inexperienced partners in the Gulf countries (Osama, 1987). Yavas et al. (1994) stated that a Saudi partner can stop his international partner from leaving the country by filing a complaint against him at the office of civil rights of the Ministry of Interior. While national laws stop Saudi partners from making untrue claims, grey areas flourish. Al-Aali (1987) claimed that Saudis believe in the power of mutual trust between the partners as the big determinant of partnership success and see its influence to be above and beyond any written contract. The Saudi businessmen, unlike their Western counterparts, do not consider the contract as the absolute determinant of a business partnership. Thus, in Saudi Arabian ventures the initial contracts are vague, not-in depth, and also subject to change by Saudi businessmen. This suggests the use of



coercive power, such as threat or the contract termination, which may lead to conflict issues negatively impacting the business performance. Dunn (1979) claimed that using threat such as negative penalty to suspend that contract due to the lack of managing the business are not working in the Gulf States due to religious and cultural traditions of these countries.

Many academics (Alon and Welsh, 2001, 2003; Welsh and Alon 2001; Sheth and Parvatiyar, 2001; Thompson and Merrilees, 2001; Pine, Zhang, and Qi, 2000) argued that franchisors should not follow consistent business models and marketing strategies abroad. Restricting master franchisees from importing raw materials from abroad can lead to other marketing issues such as higher prices. Respondent #2 stated *“It was compulsory for me to import all the stoves and refrigerators from Beirut at a high cost.”* Tuncalp (1991) stated that the master franchisee is charging the consumer higher prices in Saudi Arabia. This is because of the high import fees for the raw materials that can be easily acquired from the local markets. A similar thing occurred in Pakistan, Qureshi et al. (2018) where the John Rocket fast food restaurants charged the consumer high prices. This is because raw materials, such as meat and white onions, were being imported from the USA and the equipment for ten branches were bought upfront. The business failed due to the lack of customer demand. Welch (1992) noted that in order for international franchisors to avoid this issue, many have constructed competitive strategies to ensure quality supplies. For example, McDonald’s implemented a backward vertical integration strategy in its East European market, to make its own supply systems.

It was found in this study that the majority of master franchisees have the right to give sub-franchise. However, this is contradictory with (Alon, 2006a) who claimed master franchise strategy allows the master franchisee to exercise control. Limiting the master franchisee opportunity to involve in shaping the strategy limiting their entrepreneurial skills **raises** the level of conflict. Joint decision is very important for the progress of relationship between the franchisee and franchisor and reduce the opportunistic behaviour.

Moreover, the respondents agreed that some of the parent companies intervened in the process of hiring new staff. For example, respondent #6 stated that *‘The British and American franchisors are involved in the process of hiring key people such as the operations manager and the franchisors might request to interview them.’* This is supported by Yavas et al. (1993) who claimed that the American partners who established joint ventures with the Saudi partners

intervened in hiring policies, which lead to a control issue. The agency theory suggests that conflicts usually occur because the franchisor wants to retain control but the franchisees need more autonomy, the space to be more creative and innovative. Previous studies (Al-Motawa and Ahmed, 1996; Yavas, 1998) stated that neither coercive nor non-coercive worked as a source of power to control the Saudi agent. Manufacturers cannot apply conflict management strategies that they commonly employ in domestic settings to minimise or resolve conflicts in their international operations of the automobile industry with Saudi agents.

*‘The stick and carrot philosophy that may work in the West, does not work in the Middle East’*  
(Dunn, 1979)

The researcher noted that the Saudi franchisee companies granted exclusive rights to multiple countries such as the Gulf States, Middle Eastern countries and sometimes the MENA region or vice versa. For example, respondent #5 stated that *‘we signed a master franchise strategy with the parent company so that we would have the right to be the master franchises in the Middle East and North Africa and also to have the right to give sub franchises.’*

This could lead to further control and conflict issues with the potential franchisee in these countries. For instance, the potential franchisee needs to cope with two franchisors, the parent company and the Saudi firm that has the right to master franchise. There are some issues with the master franchise’s strategy. For instance, the master franchise format leads to administrative confusion, repetition, and incompetence. Operationally, the Saudi franchise has to cope with two franchisors – the parent firm and the company holding the master franchise –relating to the location selection, training of staffs, inspection of facilities, importation of raw materials, and promotional activities. If a disagreement arises between the franchisors over these problems, the Saudi master franchisee will find themselves in a conflict which may harm its operating plan. Involving third parties in the franchise contract or business may lead to other agency issues, such as asymmetry of information. Centralised decision-making is very important for the success of the business in the Kingdom.

Respondent #13b who deals with two franchisors stated that *‘The American franchisor were better to deal with than Kuwaiti franchisor. The Arabs are not straightforward and things are done by telephone conversations and not documented.’*

The conclusion that be derived from this study is that the controls placed by the franchisor in the contract is an issue for the success of the franchise business in the Saudi market. This may leads to the arbitration and the suspension of the contract. The master franchisee with the time gained experience and feel there is no value for running franchise business. This suggests that Agency theory issues could be examined from the perspective of entry mode strategies, such as a joint venture. The control issue also varies from sector to sector and strategy to strategy. The agency issues, such as control, can't be generalised due to the existence of different industries in Saudi Arabia. The franchisor needs to make some concessions and relinquish some power and adopt management styles that give master franchisees some freedom.

#### **6.4.5 Monitoring and Asymmetry of Information**

The agency theory suggests that the franchisors have two basic instruments to ensure franchisee collaboration: direct observation of franchisee behaviour, such as monitoring, and providing incentives and rewards to franchisee productivities. Free-riding starts when the franchisee attempts to reduce costs by providing lower quality products than specified by the franchisor, which damages the business's reputation. (Brickley et al., 1991).

The respondents agreed that international franchisors did not offer incentives or rewards to monitor the business. This suggests that franchisor may need to provide incentives or rewards such residual claimants to Saudi master franchisee to overcome this issue. Rubin (1978) and Soriano (2005) who stated that the franchisor provide incentives and rewards to reduce monitoring cost. Dunn (1979) argued that the wealth of some Arab businessmen reduce the impact of financial rewards that can be offered by the principal to the agent in the Gulf States. For instance, if the principal told their agents about a special sales promotion that could raise profits by at least \$50,000, a German agent may jump at that opportunity but many gulf businessmen would ignore it; they would rather travel to ski in Switzerland. Dant and Nasr (1998) argued that alignment of incentives is hard to do because the franchisee and the franchisor have different point of view. There is disagreement between them in selecting location and

determining price. Trust, collaboration, joint decisions and communication is vital for the franchisor to build a relationship with their Saudi partner to reduce the monitoring cost.

The restaurant managers do not receive permanent incentives from the master franchisee, or the franchisor. The restaurants managers are not following the franchise business standards and there is financial theft. For example, Respondent #19 indicated that *'Our company also experienced financial theft from the restaurant managers'*. This demonstrates that the master franchisee are shirking by not doing their job. This contradicts Rubin (1978) who claimed that franchisees do not shirk because they have ownership tied to their businesses. Dunn (1997) argued that a prospective agent in the Gulf States can promise to employ extra workers to support the manufacturer's line and later decline to do so until sales increase. The promises of the agent's organisation in the process of formation must be evaluated cautiously.

This suggests that there is a lack of monitoring from the master franchisee to follow the business which rise the possibility of shirking. If the franchisor rewards the master franchisee this will reduce the monitoring cost because the incentives of franchisor and master franchisee are better aligned than the incentives between the franchisor and hired managers. This is also indicate the relationship between restaurants managers and master franchisees are not good. This is also contradict academics Combs, Michael, and Castrogiovanni, (2004) who claimed master franchise strategy is suitable when there is a geographical distance to reduce the monitoring cost. The use of non-coercive power such as incentives from the franchisor with master franchisee could be an effective way to stop them from opportunistic behaviours

Moreover, it has been found in this study that there is a symmetry of information issue between the master franchisee and franchisor. The agency theory stresses the significance of the information transfer process between the master franchisee and the franchisor (Doherty, 1998). The respondents agreed that sharing information is essential for both the franchisee and the franchisor. Saudi Arabia has a conservative culture, people tend to be private and not share information owing to mistrust. Respondent # 4b stated *'There is a challenge for the franchisor in terms of finding experienced franchisees who are willing to share information with franchisor.'*

Dunn (1979) argued that obtaining information about prospective agents is difficult in the Gulf countries. Searching beyond the local firm's records and using traditional sources, such as the

banks and embassies, may be needed to obtain data about finances, ownership, connections, number of workers, and what other firms are represented. Many international firms rely more on shrewd observation and intuition in selecting their agents. Unreliable sources include the firm's rivals, local business owners, the agent himself, clients – local customers may have connections with the agent that the international firm is unaware of. Doherty and Quinn (1999) stated that information asymmetry is an issue in the franchise–franchisee relationship when linked to a moral hazard. The lack of transparency, enforcement of the contract, and mistrust impedes the success of the business and harms the relationship between the master franchisee and franchisor.

The absence of franchise law in the kingdom makes some of the international franchisors and potential franchisees avoid disclosing their financial and company history. Klein (1980) stated that potential franchisees need to examine the franchisor's contract and the company's past to know the number of outlets that have been terminated. Akkad (2008) mentioned that it is crucial for potential franchisee to find out about the financial status of the franchisor and how many franchisees has around the globe. It is important for the franchisor to get the master franchisee to sign a paper to stop them from disclosing confidential information before signing the contract, in case the franchisee attempts to disclose certain information about their business in Saudi Arabia.

Alsaeed (2006) assessed the level of disclosure in the annual reports of 40 Saudi companies. The findings demonstrated the disclosure index was lower than average. It was also found that company size was significantly positively linked with the level of disclosure. Aljifri (2008) examined the extent of disclosure in the annual reports of 31 listed firms in the UAE. Results showed that important differences were found among the various sectors. Alrazeen (1999) stated that the electricity firms in Saudi Arabia, on average, seem to be the best at disclosing some of the additional information which has no close relationship to mandatory disclosure, particularly information relating to employee welfare. Hutchinson (1995) claimed that for big companies, whose stocks are traded on the stock market, this information asymmetry issue recedes in importance. However, the recent inclusion of Saudi Arabia as an emerging market by the global index compiler MSCI should lead to greater transparency, and limit the asymmetry of information between the franchisee and the franchisor through corporate governance.

The researcher noted that tough competition in the local market may force the master franchisee to withhold information which affect the development of the franchise business. This study

found that that some of the interviewed companies operated multiple international restaurant brands, which may compete the each other, and these companies are more likely to conceal information from their franchisors. For example, respondent # 9b stated that *‘when we granted the right to master franchise the fashion brands which similar to each other, the franchisors were concerned about the safety of its brands.’*

Kay (1979) stated that agents in Saudi Arabia run multiple product lines, ranging from foodstuffs, toiletries, electrical appliances and automobiles to chocolate bars and computers in the Gulf States (Dunn, 1979). Nasr and Dant (1998) stated that franchisees who confront strong competition in the local marketplace are willing to gain outcomes, like customer trials, stores, and brand loyalty, than those in a less competitive marketplace. For franchisees to accomplish their aims, they tend to value any marketing advice and support offered by the franchisor. Dunn (1979) claimed that agents in the Gulf States control major lines and handle several companies so they have a track record which can be examined in some detail. Most represented firms are willing, even enthusiastic, to share information about their agents. Even rivals may be willing to share knowledge about local concerns. However, it is important to avoid local agents who handle direct competitors or too many companies. This could lead the master franchisee to shirk by exposing sensitive franchisor information.

It can be concluded from the findings that monitoring the franchise business is an issue for the franchisor. The master franchisee are not doing their job in monitoring the franchised business. The asymmetry of information, lack of transfer of information between the franchisee and the franchisor is an issue in the Saudi market. This suggests there is a lack of cooperation from the restaurant manager in term of following the company rules. This is also may indicate there is a vertical agency problem between the master franchisee and restaurants managers that led to the opportunistic behaviour. This increases the monitoring cost and impede the success of franchise business.

In summary, after examining the applicability of agency theory concepts in the Saudi context it can be said that the majority of agency theory issues apply in Saudi Arabia, except training. It is worth noting that this research has explored one sector in Saudi Arabia, and taking into consideration the differences of institutional infrastructure and organisational form common in Saudi Arabia, which is pure franchise rather than the plural form that is commonly used in

developed countries particularly United States (Technomic,1989; Bradach and Eccles, 1989) . The applicability of this theory may vary from one sector to another and differ from one entry strategy to another. It may also vary based on the type of business, organisational form, whether it is related to a service or a product. The issues which may require further investigation. Regular communication and the building strong relationships with Saudi partners, based on mutual trust, may help eliminate the agency theory issues in the absence of institutional infrastructure and law enforcement in the Kingdom.

## **6.5 Contribution to Knowledge**

The purpose of this empirical investigation was to explore the appropriateness of different franchise models in the context of an emerging market such as Saudi Arabia. Pure franchised outlets appear to be the favourite organizational form for international franchisors entering the Saudi market in the restaurant sector compared to the use of plural form that used in developed countries (Technomic, 1989; Bradach and Eccles, 1989).The results of this research provide an important contribution to knowledge regarding international franchising, particularly within the restaurant sector. This research was intended to bridge the existing gap in the literature and provide an understanding of how international franchising can play an important role in the development of SMEs, technology transfer and employment provision. There is a relationship between international franchising and the development of SMEs in Saudi Arabia. International Franchising appears to have limited impact in terms of job creation and technology transfer in this sector. Surprisingly, religion and culture appears not to be an issue for international franchisors whereas institutional uncertainty appears to be hurdle to the success of franchise business. The applicability of agency theory in the context of Saudi Arabia has been examined. As a result, payment of royalty fees, franchisee experience and business development plans, controlling, monitoring and asymmetry of information are the most significant issues that confront the potential franchisor that plans to enter the Saudi market. There are common issues which are just as relevant in the Saudi market.

The findings of this study will help academics, international franchisors, master franchisors, local franchisors, investors, social and business entrepreneurs, practitioners and policymakers to

better understand and identify barriers in the restaurant sector. Identifying the obstacles that may hinder the success of international franchising is important as the Saudi government launched its 2030 vision strategy, which aims to diversify its economy from oil, and attempts to enhance the private sector through supporting SMEs in the kingdom.

Regarding the methodological contribution of the study, this thesis used a qualitative approach to gain a richer understanding of international franchising in Saudi Arabia compared to previous studies that employed a quantitative approach (Sadi and Al-Fuzai ,2010; Sadi and Henderson ,2011; Abughazala,2006) Second, the study overcomes the previous limitations of focusing on one region of the country, the eastern province of Saudi Arabia, and focusing in multi sectors studies (Sadi and Al-Fuzai ,2010; Sadi and Henderson,2011; Chamber of commerce,2005).

### **6.5.1 Limitations**

The findings of this exploratory study should be considered as preliminary findings that need to be extended and tested, to confirm or invalidate the results. The contribution requires additional and more empirical studies on franchising business particularly the use of favourite organisational form in different sectors of franchise business in Saudi Arabia. According to Webb, (1995); Yin, (2003), research studies are limited by constraints that confront the researcher and this study is no exception. There is a lack of empirical studies and of established theoretical frameworks, relevant to international franchising, in an emerging market, such as Saudi Arabia. This study was limited to 31 Saudi companies and limited to a single geographic location and focused on one sector, the restaurant sector so the results may not be applicable to other emerging countries in the Muslim world because of cultural and religious differences. Further research is required across a variety of geographical settings and industries (Schuler, Dowling and De Cieri, 1993). The researcher found it difficult to obtain accurate and reliable economic and demographic information about Saudi Arabia, such as the population size, country GDP and the income per capita. There is a discrepancy between the published journals as well. Leonidou and Rossides (1995) note that in the majority of cases, international trade statistics and certain economic indicators are unreliable and are often out of date in the Gulf States. The impartiality of certain sources, particularly those relating to demographic statistics, is also



doubtful; great controversy surrounds the population censuses conducted out in the Gulf States. For example, the industrial classification system used in Saudi Arabia is entirely different from that of its major trading partners.

## **6.6 Implications and recommendations**

There are few studies surrounding franchising in the context of Saudi Arabia, thus, this research can be used as the basis for further studies. The findings are related to franchising in the Saudi restaurant sector. This research can provide recommendations and insights into the Saudi Arabian market, for local franchisors and international franchisors who are interested in conducting business in Saudi Arabia. The concept of franchising is relatively new to Saudi Arabian companies but there is great potential. The Saudi franchisee should invest in well-known brands and focus more on the franchisor's experience and brand reputation and find more information about the business through the associations that it is a member of. The majority of franchised businesses are western brands so the master franchisee may need to turn to Asian brands such as Chinese, Korean, Japanese and Singaporean, since these countries are well-known for having advanced technology, as compared to their western counterparts and vary their investment in different sectors, particularly ones which export high technology. Since the establishment of the general entertainment authority by the Saudi government and lifting of the ban on movie theatres and cinemas, the master franchisee should diversify their investment in different sectors, such as education, travel agencies, lodges, hospitality, spas, salons, gyms, motels, gas stations, event management and conference leisure and entertainment sectors. The diversity of the Saudi society and cities with a large number of expatriates require more sector diversification to meet the people needs and demands. For example, Mecca and Medina city hosts a large number of pilgrimages, so retail, hospitality, transportation, museums and barbershop salons are worth investing in.

### **6.6.1 Recommendations for public authorities and institutional stakeholders**

Saudi Arabia is the 12th largest country in the world and has a strategic location that connects the country with Africa, Asia and Europe, so for the master franchisee investing in the service sector, such as transportation, ports and airports, will improve infrastructure and reduce the duration of the goods staying stuck in Saudi customs; also this sector may transfer technology, as compared to the restaurant sector. The Saudi government needs to ease the bureaucracy of its internal regulations, such as regional municipality, the Ministry of Labour etc., and improve its judicial system by establishing a franchise law which will encourage and push for more Saudi lawyers to specialise in franchising law and running consultancy services that will help to develop local concept.

The existence of a franchise law will attract more international franchisors and enhance the transparency and trust in the Saudi judicial legal system. This will lead to zero anxieties regarding intellectual property, strengthen the relationship and trust between the two parties – the franchisee and the franchisor – and encourage the local franchisor and the master franchisee to grant a master franchise or sub-franchise, which will reflect positively on supporting entrepreneurs, allowing quick business development plans and providing jobs. In addition, this will encourage and provide the master franchisee the power to implement arbitration in Saudi Arabia. The establishment of a franchise association will be a platform between the franchisee, the franchisors, consultants, businessmen and the international franchise associations, in terms of exchanging information and culture and encouraging creativity. It is also a place to provide the international franchisor with current, accurate and reliable information about the franchising industry in Saudi Arabia. This will increase the level of transparency and limit the asymmetry of information. The establishment of local franchise associations will educate the entrepreneurs about franchising business models as a tool for starting a business venture.

The local franchise companies should visit Saudi schools to break the social stigma by providing the example of local role models, such as the owners of Albaik and Altazaj (famous Saudi local brands), this will inspire and encourage students to work in restaurants. For example, the majority of master franchisees have the right to grant sub-franchise, so there is a way (conditional contract) of benefiting from this by hiring citizens to work in one of the franchisee's

restaurants. With time, these citizens can be promoted to managerial positions, following which become a sub franchisee by implementing this strategy will become a source of job creation, providing entrepreneurship skills so that well-experienced sub franchisees can meet the master franchisee expectations.

The businesses administration colleges should teach franchising curriculum to increase awareness regarding the importance of franchising as a catalyst of economic development. The Saudi Chamber of Commerce needs to conduct more workshops and seminars in different cities and not just focus on certain cities, such as Riyadh, Al-khobar and Jeddah, and need to host international franchise exhibition to teach citizens and increase public awareness about the important of franchising. In order for SMEs to grow, the government should provide prime location priority to smaller local enterprises to protect them and help them progress since these prime locations are controlled by companies that have huge amounts of money.

Financial institutions and banks should support local entrepreneurs who are interested in the franchise businesses to help spread the benefits of the model. This is also a secure investment for the banks because of the high chance of getting the returns on investments compared to running local business. The Ministry of Labour and Chamber of Commerce also needs to restrict the royalty fees percentage to 5% since this study found many infamous international franchisors brands asking for higher fees. The Saudi Chamber of Commerce should not register any international franchise with less than ten years of experience to allow the master franchisee to fully benefit from the business model. The establishment of specialised franchising educational centres for the education of Saudi businessmen and potential franchisors on how to operate their businesses is essential. Also the establishment of institutes to train citizens in the occupations required the by restaurant sector, such as chef, waiters and cashiers, in order to prepare them for the market job and bridge the gap in finding qualified staff.

### **6.6.2 Recommendations for potential investors**

This empirical investigation provides insights and suggestions for potential franchisors, social and business entrepreneurs and international companies thinking to open and operate international franchise businesses within different sector in Saudi Arabia. The master franchise

appears to be a suitable strategy for an international franchisor to enter the Saudi market. Through this strategy the franchisor does not need to deal with many partners which may limit the agency issues such as shirking, centralisation and free riding. Through this strategy potential franchisors can penetrate neighbouring countries as the economic integration between Saudi Arabia and other gulf states will allow the movement of goods through unified customs, religion and culture similarities which present potential opportunities to potential investors to these lucrative markets with a high disposable income and population growth.

The franchisor needs to locate their regional offices in Saudi Arabia instead of establishing them in neighbouring countries or other Asian countries. This will allow the regional supervisor to monitor the franchise business closely and provide any training and assistance that needed. This will save travel time and eliminate monitoring cost. In addition the regional supervisor plays a vital role in enhancing the relationship between the franchise and franchisor once a problem arise.

It is important for international franchisors and investors to consult with local lawyers and consultants who are bilinguals to avoid language issue and regarding the brand registration in the Ministry of Commerce to protect their trade mark and intellectual property in a country where there is no franchise law and a lack of specialised lawyers in franchising. The use of mixed strategies such as a joint venture and master franchise may be an effective tool to overcome the issue of intellectual property protection by testing the market and controlling the business through joint venture strategy while delegating some of responsibilities to the potential master franchisee through the franchise strategy. In the absence of franchise law and the weakness of enforcing the contract in Saudi Arabia, the honesty and transparency between the potential franchisor and master franchise is important regarding to Uniform Franchise Offering Circular (A franchise disclosure document). In addition, it is important for the franchisor to implement arbitration in neutral region which will be considered a satisfactory for both parties to avoid an issue. The experience of the master franchisee (local knowledge, work ethics) is essential for the success of the franchise business so having a master franchisee who has expertise in managing a franchise is important for the franchisor and avoiding any potential master franchisee who operates more than international brands which limit the issue of asymmetry of information. The franchisor should treat the potential master franchisees a partner not an employee and see him as

a partner in solving problems. Sharing decisions and team working is important for the success of the business. Creativity, franchisor expertise, ability to predict, consumer behaviour studies and brand development are vital to meet the tough competition in a buyers market such as Saudi Arabia where price is important to meet the tough competition. The equal investment of both the franchisor and potential master franchisee needed and financial capability of potential franchisor is important for competing rivals and meeting the business development plan. This is will reduce costs and increase productivity and profitability.

Intelligence, marketing research and feasibility studies are important for potential franchisors and investors to project and to determine the potential risk whether politically such as war in Yemen, Iranian proxy war, Qatar blockade, the expel of Canadian Ambassador which may stop the movement of goods and cause a delay in the delivery of items or economically such as the plunge of oil prices and low economic growth, this may lead to cost cutting such as food cost , laying off staff , low salaries which affect negatively in the quality of service and product. The purchasing power of Saudi citizens and level of city infrastructure differs from one city to another. Targeting populated regions with large populations (diversity, high level of accepting foreign brands) and good infrastructure (logistic support) is important for the success of franchise business. Paying attention to hidden costs such outlet decor, training, outlet location, hiring and importing raw material are essential, especially in the beginning phase to avoid issues that relate to agency problems such as the inability of the master franchisee to pay the royalty fees.

Franchising is limited to certain sectors such as restaurants and retail in Saudi Arabia which somehow demonstrates the ignorance of Saudi businessmen about franchising. There are around 65 franchise businesses activities opportunities where the franchisor can invest in them in Saudi Arabia. Saudization appears an issue for both the master franchisee and international franchisor in the restaurant sector when it comes to hiring qualified staff or when it comes to business expansion. However, it would be a good idea for potential franchisors to hire Saudis in the top positions such as operation mangers, restaurant manager etc to avoid high turnover and cultural misunderstandings in this sector. It is worth noting that saudization may not be an issue in different sectors such as retailing and hospitality.

The percentage of sales dropped sharply in Ramadan (Holy Month) for the majority of restaurants so the master franchisees committed to pay the royalty fees and to pay the overheads such as electricity, property rent and staff salaries. It would be a good idea for potential investors to allow the potential franchisee to give some the staff break (vacation) to avoid paying salary and save cost on electricity. Standardised product, advertising and service is not working in Saudi Arabia. The potential franchisor and investors need to adapt their services and products to the norms and culture of the country. That means the possibility of relinquish the power and concessions .It is worth mentioning that consumer habits and demands change over time through traveling and demographic shift.

Doing business with local companies who are real estate developers makes it much easier for potential investors to find the appropriate location and avoid dilemmas such as the suspension of the ownership and dealing with property landlords such as raising rent or selling the property. Finally, the establishment of the company supply chains (vertical integration) in Saudi Arabia will allow these potential entities to deal with local SMEs through the kingdom through providing raw materials at lower cost, avoiding high fees of Saudi customs, expiry dates, halal items and the long length of delivery along with other issue that may arise such as the ban impose by food and drug authority on certain items. The foundation of supply chains goes in line with the Saudi vision 2030 through supporting the private sector through the development of SMES and creating jobs for Saudi citizens. This will also allow for these companies to benefit from the incentives that the Saudi government offers such as tax exemption, free property land and electricity due to the gas resource availability in the country. This also avoids the issue of dealing with the bureaucratic system of Saudi customs and clearance of the items.

### **6.6.3 Recommendations for Further Research**

This study has identified a few areas that could be explored through further research, especially with the current social and economic changes in Saudi Arabia. With the government lifting the ban on women driving and reducing the power of the religious police, women can be involved in

the workplace and be allowed to work in restaurants, etc. Furthermore, the lifting of the ban on cinemas and the change of consumer behaviour through traveling for education abroad, utilising the King Salman program scholarship opens up new avenues to look into. It would more valuable if this study was updated to the current changes in Saudi Arabia. International marketers should keep in mind that the marketing situation in the Gulf countries is very dynamic and that marketing plans should not stay static but should be revised consistently (Leonidou,1991).

There is a need for more studies to be conducted to explore the suitable organizational form and the role of international franchising on economic development within the context of Saudi Arabian restaurants, employing a qualitative approach to build theory and using a quantitative approach to test the findings. It would be interesting if this study was extended to neighbouring countries, such as Kuwait, or another Gulf country to contrast the findings. The generality of this study could be also tested in countries of a similar cultural, religious, political and economic level such as the Gulf States.

The researcher recommends further empirical studies to be carried out on specific categories of the restaurant sector, such as quick-service restaurants and casual dining restaurants. There is also a need for research to be conducted in different sectors, such as retail, entertainment and fitness, using a qualitative approach, because there are none or few studies on these sectors. Further investigation and exploration of the retailing sector is required since research companies, such as BMI and Mackenzie, predict that the retail sector will contribute to the economic development of Saudi in terms of job creation. This study can be duplicated for several sectors such as retailing, hospitality, etc. The researcher also emphasised the need for more exploratory studies on the social impact of international franchising from the perspective of the owners of local restaurants and the consumer perspective. The impact of international franchising on Saudi women entrepreneurs need to be investigated in different sectors. In addition, empirical studies are needed to compare the experience of SMEs who adopted the franchise model in the restaurant sector with SMEs that did not. There is a need for empirical studies to apply agency and exchange theories to the operation of multiple brands by a master franchisee within one

sector, such as restaurants, to explore the conceptual issues. Additionally the applicability of agency theory may be examined in relation to the link between a domestic franchisee and a franchisor in Saudi Arabia.



## **Appendix (1)**

### **Restaurants Sector in Saudi Arabia**

The fast food sector plays an important role in providing employment, economic growth and human resource competency, with over 240,000 locations in the United States and sales of over \$206.3 billion in 2016 (Statista, 2016). Sang-Kyun, (1994) mentioned that the fast food restaurant sector is one of the fastest growing industries in many emerging economies. Authors claim that the number of fast food restaurants is increasing because of increases in income, changing lifestyles, the involvement of women in the labour market, the young generation's curiosity to try new things and the rising number of international fast food restaurants in the emerging markets (Kucuhemiroglu, Kaynak, and AKsoy, 1996; Sang-Kyun, 1994). McDonald's, Hardee's, Burger King, Wendy's, KFC, Pizza Hut, Domino's, Popeye's chicken, Sizzler's, Denny's, and Taco Be11 are considered the biggest brands in the fast food sector in emerging economies (Price, 1993a; Sang-Kyun, 1994).

The Gulf States are one of the largest markets for fast food (Randheer and Al-Aali, 2015). A report released by Al Masah Capital, a leading alternative asset administration and counselling company in Middle East, reported that the Gulf countries' food service market is projected to increase at a compound annual growth rate (CAGR) of 8% to \$29.3 billion by 2020, up from \$21.5 billion in 2016 and \$20.1 billion in 2015. The fast food segment grew by 7.4% and has been predicted to maintain its leading position in the market followed by the full service restaurant segment which grew by 6% CAGR. The Cafes and bakery segments, whose sales expanded with a CAGR of 7.5% between 2012 and 2016, are also expected to grow at around 3% CAGR to reach \$2.75 billion by 2020 (Al Masah Capital, 2017). Fast food chains form the largest segment of the franchise market in Saudi Arabia. In 2014, there were 14,366 fast food outlets in Saudi Arabia (Basahih, 2013) (See Table16.). A report by Euromonitor International on the Saudi fast food sector reported the total number of fast food outlets at 14,366 in 2014 a rise of about 11% over 2009. The total profits gained by these outlets was valued at about \$5.7 billion, an increase of 60% over 2009. It has been forecasted that sales from the fast food subsector would exceed \$7 billion by 2020 (Mousa, 2013).

According to a Gulf Council Countries food service report, the market volume of Saudi quick service restaurants was worth \$5.1 billion in 2015. It is the biggest fast food restaurant market (with 43.8% share) in the gulf countries. (Saudi Gazette, 2018). According to BMI, the fast food sector in Saudi Arabia will grow because of the increasing purchasing power among Saudi people, which allows them to dine out as an entertainment activity. International fast food giant McDonald's is still the biggest the fast food outlets in Saudi Arabia. The company is run by Riyadh International Catering Corp and established its first outlets in 1993. There are 134 restaurants in the Kingdom along with other global brands, such as KFC and Pizza Hut (Saudi Arabia Food and Drink Report, 2018).

The demand for fast food is increasing due to changing lifestyles and the influence of western culture, the increase in female workers in the labour market and access to different of fast food selections. However, the consumption of fast food is becoming a concern to the companies to offer healthy options in the menu. 6Wresearch stated that hamburgers and sandwiches form most of the market share of fast food in Saudi Arabia due to the consumer taste preferences and increase in demand from young citizens. Another major factor is the shifts in habit to eating out which is projected to lead the market of fast food during 2017-2023. The take away restaurants are the biggest selling fast food outlets in Saudi Arabia due to fast service, good network to approach and adaptability to the local demands and culture. Fast food trucks are becoming a trend in the market due to the growth social occasions such as food festivals. The Asian and Latin American food demand is also increasing due to the increased number international tourists. Riyadh and Jeddah city, the hub for tourism had the biggest market share of fast food, with McDonald's, Dominos, Pizza Hut, Burger King, Herfy, KFC and Al Baik all present (Jat, 2018).

The numerous fast food restaurants in KSA can be attributed to reasons such as brand awareness, expatriate inhabitants and a big population of young Saudi citizens (Randheer and Al-Aali, 2015). The shift in demographics from an older generation to a younger consumer market is a key factor in encouraging international companies to invest in Saudi Arabia (Abdul Cader, 2012). The young customer market is more sustainable than the older customers (Gunter and Furnham, 1998).

The change in lifestyle of the Saudi people due to economic growth has led to a cultural change towards a more developed global standard of living which has impacted food selections and consumption habits (Al-Othaimen et al, 2007; Sadi, and Saricimen, 2010). Saudi Arabia's open-door and free-market policy has led international fast food companies, including the U.S. fast food companies, to enter the market to satisfy consumer demand in Saudi Arabia (Bhuian, 1996b). The young generation has a strong interest and preference for foreign brands of fast food restaurants (Bhuian, 1996a). As a result, there is higher consumption of fast foods by Saudi Arabians, particularly young individuals (Collison et al; 2010). Most Saudi Arabian families with children like to dine at restaurants as they are considered the best places to spend time, and they have money to dine out. They usually like to dine during the evenings, weekends and holidays due to climate (hot, cold weather). Another reason for this is the absence of alternative entertainments. (Al-Othaimen et al.; 2007). However, Saudi Arabia declared the return of the cinema and movie theatres after being closed down for almost 35 years (Arab News, 2017).

Many Saudis travel abroad and have been exposed to western and foreign brands which provide different types of food (Mousa, 2013). Moreover, there are many expatriates who reside and work in Saudi Arabia which also led to the boom of international restaurants. The high demands for fast food restaurants from citizens and the large number of foreigners have coerced Saudi businessmen to invest in the restaurant sector (Al-Zahrani and Hasan, 2008).

Bhuian (2000) investigated the characteristics of fast food restaurants that affect customer preferences in Saudi Arabia. This study found that the nutrition, price, taste, speed, variety, seating capacity, location, novelties, friendliness and cleanliness influence customers in Saudi Arabia although delivery service is not important to consumers in Saudi Arabia. Azzam (1995) and Tunji (2000) argued that people in Saudi Arabia tend to be close to their families and their family size is big so they like to have a cosy homes; therefore, the delivery service is considered convenient for them as they prefer staying home and having nice meals with their loves ones. Al-Maneena (1995) mentioned that eating capacity in restaurants is too high among the Saudis for them to a select restaurant. Saudis like to hang out in restaurants either with their family or with colleagues. Finally, findings of this study also indicated that there is a similarity in culture,

technology and anthropology between the Gulf countries which make it easier for foreign investors in the restaurants to enter it (Baker and Abou-Ismaïl, 1993).

Almohaimmeed (2017) investigated the influence of international restaurant quality on consumer satisfaction in Saudi Arabia. Restaurant quality is based on halal food, hygiene, menu and atmospheric quality as well as assurance, accuracy, responsiveness, interior design, external environment and price. This study suggested that restaurant owners in Saudi Arabia should pay attention to the halal quality and avoid any use of non-halal products. In addition, they should focus on food quality such as taste, freshness and quantity of food, hygiene, clean dining place, hiring clean employees who are responsive and knowledgeable about the items and having menu that contains a variety of dishes. A study conducted by Eid (2011) investigated consumer loyalty in Saudi Arabia's in restaurants. This study concluded that consumer satisfaction is highly influenced by customer loyalty (Eid, 2011) and the customer's inclination to buy in the future (Saaty, 2011). Sadi and Saricimen (2010) examined the features that influence consumer satisfaction in the restaurant market in the eastern province of Saudi Arabia, and claimed that factors such as service quality, product quality and physical appearance have an important influence on consumer satisfaction. However, the product price does not seem to affect consumer satisfaction. DiPietro (2003) claimed that in the fast food sector, there is a strong relationship between consumer satisfaction and profits over time.

A study conducted by the Chambers of Commerce (2005) showed that Saudi consumers generally prefer foreign brands in different sectors such as clothing, cosmetics, household and office furniture, electrical appliances, telecommunications, medicines and medical equipment, and similar statistics were found for restaurants, fast food and beverages. The factors influencing consumer purchasing decisions are as follows: personal experience, family and friends, and television and radio advertising. As for the impact of the social situation in the purchase decision, the quality factor was affected by the brand, followed by the price and service, in the preference between international or local brands. The preference of foreign brands among the Saudi citizens is make it easier for international franchisors to enter the market.

Tunsi (2000) investigated consumer loyalty in international restaurants in Saudi Arabia. The study concluded that Saudis consider home delivery service as a significant factor that influences

their decision to be a loyal customer. The study also found that the loyalty of Saudi customers is impacted by the interior design of the restaurant. They appreciated restaurants that offer private partitions, as they tend to seek privacy when eating out with the family. Customer expectations are high, therefore, more than decent quality and low prices, consumer loyalty is getting tougher to accomplish and maintain (Alshaya, 2001).

The international food giant McDonald's hired 4,000 young Saudi men as part of its move to expand operations, targeting young graduate students, so that the company can provide them with essential skills and training. The Saudi youngsters were employed by McDonald's within 30 months (Khan, 2014). According to 2012 data released by Saudi Central Department of Statistics and Information, 647,000 Saudi women were hired in 2012, which is 86% more than 347,370 in 1999. Since mid-2012, females are permitted to work in shops and retail stores for the first time in Saudi Arabia's history. Saudi females can now work in lingerie and makeup shops, as supermarket cashiers and at factories in female's only sections without mingling with men in the workplace (Mousa, 2015). According to the local Saudi Al-Madinah Arabic newspaper, the Council of Saudi Chambers is planning to hire females in the restaurants sector. They plan to employ females in 16 restaurants. They will conduct a workshop with the restaurant owners to discuss strategies to employ more females in this sector (Saudi Gazette, 2018).

It is a huge challenge for the training division to make sure training yields satisfactory outcomes and provides a return on investment in the fast food sector (DiPietro, 2003). For instance, Hartvigson and Hourani (2009) claimed that most Saudi citizen feel ashamed of working in low class jobs such as at coffee shops, restaurants and hotels. Alromi (2000) mentioned that most Saudis would choose to make a low salary in a white-collar position than a high salary in a blue-collar position. According to Ramady (2010), Saudi citizens are unwilling to do physical work and their social status is very important for the young generation which influences their social relations and prospects for marriage. Bell (2005) claimed that Saudis are not interested in working at restaurants which negatively impacted the international franchisors while recruiting Saudi citizens because the locals are more encouraged by status and position. *'Many young Saudis have grown up in luxury, seeing their parents getting well-paid, high-status positions'* (Bell, 2005).

Saudi employees are not interested in working in lower-class positions (Rowings et al., 1986; cited in Idris, 2007). A new report indicates that one fourth of Saudi workers in the private sector do not regularly come to work which leads to a high turnover rate (Al-Kibis et al., 2007). The majority of Saudis like to be hired for managerial positions. Lower class positions are seen as undesirable and shameful. This is profoundly engrained to the degree that families and the government encourage those who overcome these socially unaccepted positions (Yadav, 2005). Gresh (2000) stated that the Saudization added a cost factor to local companies and did not succeed in encouraging Saudis to work at low positions. The author argued that foreign workers cost less, follow the company rules, are punctual and are willing to work six days a week. Richards (2001) argued that the difficulty of finding jobs has compelled them to accept jobs such as receptionists, kitchen staff and restaurant cashiers

**Table 16. The Number of Outlets and Revenues of Fast Food Restaurants in Saudi Arabia in 2014**

| <b>Type of Fast Food Restaurants</b> | <b>Number of Outlets</b> | <b>Sales Revenues in Value in Millions of US\$</b> |
|--------------------------------------|--------------------------|--|
| Bakery Products Fast Food            | 7,949                    | \$1,643.9  |
| Burger Fast Food                     | 1,230                    | 1,516.8  |
| Middle Eastern Fast Food             | 1,697                    | 1080.3   |
| Chicken Fast Food                    | 979                      | 458.1  |
| Other Fast Food                      | 788                      | 351.1  |
| Convenience Stores Fast Food         | 486                      | 133.9  |
| Ice Cream Fast Food                  | 897                      | 317.0  |
| Asian Fast Food                      | 266                      | 131.2  |
| Latin American Fast Food             | 74                       | 22.0   |
| <b>Total</b>                         | <b>14,366</b>            | <b>\$5,654</b>                                     |

Source: (Mousa, 2015)

## **Appendix (2)**

### **Consent Letter**

**Dear Sir,**

I would like to invite you to take part in my PhD research which aims to explore the appropriateness of different franchise models in the context of Saudi Arabia focusing on the restaurant sector.

#### **About the study**

The goal of my study is to explore the role of international franchising in the development of SMES, entrepreneurial and managerial skills development, technology transfer and reduction of unemployment. I also to explore the barriers that may impede the success of international franchising such as religion, culture and country regulations. I am also looking to examine the relationship between the franchisee and franchisor focusing on the restaurant sector.

#### **Your involvement in the study**

I would like to conduct an interview with you in order to hear your perspectives and experiences on this topic. If you are able to spare some of your valuable time for an interview, I am sure your remarks and comments will be of great value to the study. The duration for the interview would be one hour, and with your permission, I would like to make an audio recording of the same.

Your inputs will be confidential. The data will not be shared with the other respondents and your comments will be treated anonymously. Some comments may be reported in my PhD thesis and in any subsequent academic publications, but they will only be attributed to 'Respondent 1, 2, 3, etc'. Your participation is voluntary, and you have the right to withdraw from the interview at any given time without any explanation.

If you have any further questions about this study or the research process please contacts me or my supervisor, Professor Steve Burt, at the School of Management at the University of Stirling:

Kind regards,

Abdulaziz Alotaibi

**Supervisor Name:** Professor Steve Burt

Contact: [s.l.burt@stir.ac.uk](mailto:s.l.burt@stir.ac.uk)

**Researcher Name:** Abdulaziz Alotaibi

Contact: [a.k.alotaibi@stir.ac.uk](mailto:a.k.alotaibi@stir.ac.uk)



## Appendix (3)

### Survey Instrument Guides

Interviewee's Name:

Position:

1- Do you think international franchising has positive role in terms of the following?

- Growth of small and medium enterprises in the restaurant sector?
- Developing managerial skills?
- Technology transfer?
- Any other comments would you like to add?

2-Do you think international franchising business has a positive role in terms of the following:

- Job creation?
- Any other comments would you like to add?

3- Does international franchising contribute to the emergence of entrepreneurship in restaurant sector in terms of the following?

- Empowering Saudi male/female entrepreneurs?
- Enhancing innovation?
- Increase competition?
- Any other comments would you like to add regarding to this question?

4-The penetration of new market could be a challenge for the potential international franchisors.

- Are there any specific strategy/format to enter the market?
- Have franchisor experienced issues related to the following:
  - Religion?
  - Culture?
  - Law and regulations?

-Any other comments would you like to add?

5-Are there any specific problems you confront with the partner you are associated with? Do any of the following apply to you?

- Royalty fees
- Training
- Franchisee experience

- Controlling
- Monitoring
- Sharing information
- Any other comments on the franchise and franchisor relationship you would like to add?

Thank you for your participation.

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