Confidential

Business format franchising – The next market entry model for Boots Retail International?

By

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Executive Summary

This dissertation is based in the field of international retailing and in particular, the value and challenges associated with employing franchising as a vehicle for international retail expansion. Its focus is on The Boots Group (TBG) and specifically its loss-making subsidiary BRI (Boots Retail International).

Despite its loss-making label, BRI is currently enjoying a significant upturn in fortune, on the back of very positive profitable growth figures, which have generated an increased enthusiasm for expanding the number of markets BRI is currently actively trading in. This has lead to the challenge of investigating whether BRI should develop a retail business format franchise for application as a relatively risk free method of market entry and if so what market offers the best option for testing this franchise system.

The methodology for the research used to answering this challenge utilises, a literature review and contemporary practitioner interviews, to establish and refine a series of hypotheses for the factors critical to successful franchising. These factors are tested against the Boots retail model to provide an insight into the feasibility, benefits and risks of its use as the basis for a franchise system.

Having established the potential value of developing a franchise system the study looks at the factors which characterise successful franchise markets and, using quantitative data, partially validates an internal belief that the Middle East markets, specifically the GCC present the best opportunity for testing the system. Further data is then gathered utilising inputs from potential franchisees to complete a full strategic market analysis and operating model for a Boots franchise system in the region.

This study concludes that Boots should, through BRI, develop a retail franchise system and that this system should be tested in the GCC markets as a prelude to a full roll out in this market and its application as a model of market entry which compliments the existing ‘implant’ strategy being used to great effect within BRI.

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Chapter 1

Introduction

1. Prelude

This chapter introduces this report. The rationale for the study is explained against a backdrop of the turbulent history of the Boots Retail International (BRI) business. It explains why a number of concurrent conditions have created an opportunity to investigate the potential of extending the BRI business model and describes the full objectives for this piece of research and analysis, as well as an overview of its presentation.

2. Rationale for this study

i. Introduction to Boots Retail International

BRI was established as a separate legal subsidiary within The Boots Group (TBG) in 1996. At this time the major profit contribution (in excess of 85% of group operating profit) was provided through the 'cash cow', Boots The Chemists (BTC), the UK health and beauty[1] (H&B) retail chain. In 1996, the BTC portfolio extended to 1250 locations, generating an annual turnover of just above £3.1bn, founded on its history spanning a 150 years, which cemented the chain as 'Chemists to the Nation'.

The BRI structure encompassed the small but successful Boots Beauty International (BBI) business that provided the Group with a profitable export business based around No 7 cosmetics. Its creation followed a number of 'sub-optimal' attempts at international expansion that included the operation of a Canadian drugstore chain (halted in 1990) and the French beauty subsidiary Sephora (sold shortly afterwards).

[1] Beauty is defined as including toiletries, cosmetics (mass and premium) and all fragrance for the purposes of this dissertation.

The initial concept whilst continuing to support the existing BBI business, involved copying the UK BTC 'three in one'[2] retail model and commenced in 1997, through pilots in Thailand (BRT) and Holland. Additional stores were opened in Thailand during 1998, followed by representations in Japan (1999) as part of a joint venture (JV) with Mitsubishi.

Replicating the BTC store model required a significant capital investment necessitating initial losses (table 1), which caused little concern, having been originally provisioned as part of the value case. However by the end of the 2000, despite the most encouraging launch to date, Taiwan, it was clear that the model was failing and its losses couldn't continue.

	Group Turn-over (£M)	Group Operating Profit (£M)	Turn-over Growth (% inc vrs. LY)	Operating Profit Growth (% inc vrs. LY)	BRI Turn-over (£M)	BRI Profit (£M)	Turn-over Growth (% inc vrs. LY)	Operating Profit Growth (% inc vrs. LY)
1993/1994	4167	488						
1994/1995	4308	520	3.4%	6.6%				
1995/1996	4125	443	-4.2%	-14.8%		-1.1		
1996/1997	4578	492	11.0%	11.1%		-8.5		-672.7%
1997/1998	5022	538	9.7%	9.3%	5.2	-21.2		-149.4%
1998/1999	5045	562	0.5%	4.5%	15.8	-20.9	203.8%	1.4%
1999/2000	5189	565	2.9%	0.5%	32.5	-32.6	105.7%	-56.0%
2000/2001	5226	581	0.7%	2.8%	42.1	-43.9	29.5%	-34.7%
2001/2002	5332	626	2.0%	7.7%	40.3	-24.1	-4.3%	45.1%
2002/2003	5322	544	-0.2%	-15.1%	37.0	-22.3	-8.2%	7.5%
2003/2004	5326	550	0.1%	1.1%	43.0	-10.4	16.2%	53.4%

Source: Group Accounts

Table 1. Group and BRI ten year performance

TBG reviewed the investment over the initial 5-year period and chose, before resorting to closure, to appoint a new management team charged with developing options to turn the BRI business around. Further international store development plans were put on hold and an agreement was reached to sell off the Dutch stores whilst this new team undertook a detailed analysis of the original model and explored the reasons for its failure. This

[2] 'Three in one' referred to the combination of three major categories, Health, Beauty and Personal Care that sat at the core of the BTC customer offer.

investigation spawned a new business proposal based on a concession or 'implant' model (covering around $40m^2$) containing up to 900 differentiated and exclusive products, which became known as the 'Core Global Inventory' (CGI).

The implant provided a mechanic to export differentiated, high margin, Boots inventory to international partners with BRI agreeing to support consultant training and provide merchandising guidance as part of the relationship. The implants were tested through two formats in Thailand and Taiwan, stand-alone $40m^2$ - $60m^2$ stores (utilising the existing portfolio) and through partnership with a major drugstore competitor, Watson's

Following this successful trial TBG signed off a transition plan comprised of the first new implant market implementation (Hong Kong) and a restructure of the Asian retail operation. This included dissolving the Japanese JV and rationalising the Thai inventory, facilitating a reduction in store sizes and costs.

The application of the implant model has provided BRI with a more sustainable route into international markets. Most recently it has enabled entry into the potentially huge American market via pilots in partnership with two organisations, CVS Pharmacy and Target. The potential of this market has meant that it has been the major point of focus for the business over the past 12-18 months and this attention has been rewarded with Group board approval to progress to the second pilot stage, taking the number of implants in America to 141 (June 2005).

The most significant benefit of the implant model is that it can be implemented through a significantly lower level of capital investment with a commensurate lower level of risk. The proposition occupies existing retail space in partner stores and allows BRI to reduce cash tied up in stock as the CGI consists of a smaller number of stock keeping units (SKUs) than the original full retail model[3]. Consequently, BRI has been able to lever the implant model, rationalisation in Thailand and the further extension of the export offer, to reduce its loses. The latest financial results illustrate this with all countries making a profit (excluding the new USA pilot) and BRI delivering a 20% growth in like for like sales.

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[3] A important element of this reduced stock holding is that BRI has been able to pull the non CGI SKUs for Thailand (known as the Thailand only Inventory, TOI) directly from the BTC warehouse levering the scale of the now 1400 strong UK chain.

The BRI portfolio, depicted in part in figure 1, now extends to include consolidated space within other retailers, or wholly owned stores in 13 countries. Operations are supported by teams based in Hong Kong, Taiwan, Thailand, USA and Switzerland, in additional to a central support and brand exports teams in Nottingham.

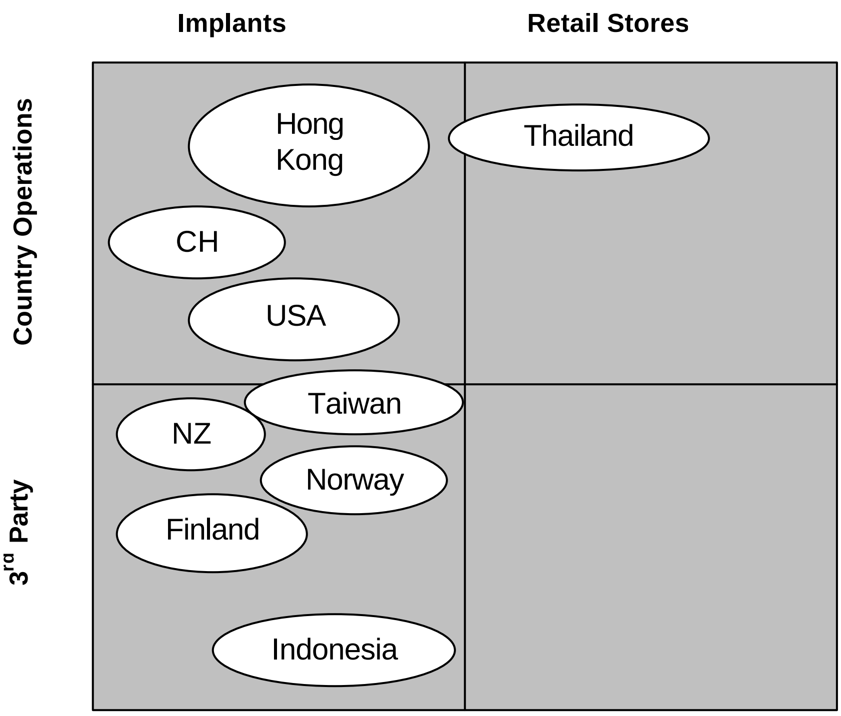

Figure 1. Illustration of the distribution of markets within the current BRI portfolio

ii. An additional model of market entry?

TBG has recently announced its decision to sell Boots Healthcare International (BHI) and when this sale is completed BRI will be the only route for international business within the Group. The recent improvement in BRI's performance has generated challenges to further extend the distribution of implants and whilst this is great news for the business a recent review of other global market opportunities has indicated that the implant model may not always be the best market entry model; e.g. in less developed markets, characterised by retail H&B fragmentation, or markets where the Boots brand enjoys high levels of awareness.

The above 'two by two' representation of the current BRI portfolio also starts to highlight that there may be a more lucrative model for markets characterised by existing brand equity. This research presents the argument that a full retail proposition could provide the basis for this model, however such a posit sits against the absence of any countries within the bottom right box. This gap reiterates the fact that since being severely burned in Japan, BRI has steered away from fully branded retail stores owned by or in partnership with 3rd parties.

Hence this report must contend with BRI's unfavourable full retail experiences, which have fuelled the subsidiary's evolution from largely unsuccessful retail stores into more successful internationalisation via the implants. This strategic shift has been accompanied by significant reductions in personnel, leaving a small team focused on, and competent in, the delivery of implant businesses[4]. This creates a dilemma, in that though there may well be an opportunity to create an additional market entry model, doing so may stretch the small resources too far and could jeopardise the success of the US expansion, upon which much of BRI's future profitability is predicated. The obvious solution of simply recruiting more resource is not a feasible option for BRI, as it must maintain a low cost base to support its imperative for survival, i.e. to deliver a positive contribution to group profits.

This strategic dilemma is similar to the mountaineering 'Death Zone' metaphor outlined by Starkey (2005). He suggests that organisations run the risk of experiencing the same disastrous outcomes as climbers who stretch their resources too thin when they are blinded by 'summit fever'. This metaphor is particularly relevant to BRI's current climb to profitability as the introduction of a new entry model capable of faster returns may expedite this ascension, however such an expedition fuelled by such summit fever may also serve as a fatal banana skin if the organisation ignores its limits in a push for the final goal.

[4] Thailand remains the exception to this position with the Thai business (BRT) having its own dedicated staff extending to around 700 personnel across Head Office in Bangkok and the 80 stores across the country.

iii. Why consider franchising as an additional model?

The previous section has highlighted the potential opportunity to develop a model of market entry based on a retail store format and set out the rationale for a key criterion of any model in that it must not require a significant level of financial investment. This criterion is a primary driver for the decision to further investigate franchising.

In developing his theories on why franchise companies expand overseas, Shane (1996) references the views of Hymer and Caves, who argue that companies levering a domestic proprietary advantage through little, or no additional cost possess a strong foundation for global expansion. They suggest that a franchise system is an example of this type of proprietary advantage and such a system could provide BRI with a low risk entry model, which introduces full retail participation via the Boots retail brand.

TBG currently operates a small number of business format franchises within its opticians chain, Boots Opticians Limited (BOL), but has never progressed thinking on franchising a BTC format. However a significant assertion underpinning this research is that the success of the remodelled Thai stores indicates that a franchise system could be developed which provides BRI with an additional market entry model. Such a system should be more profitable than implants, whilst retaining the important features of reduced risk and minimal capital investment requirements.

Further, one can hypothesise that, a successful franchise system could be of huge strategic importance to BRI at this present moment in time, as it would support lower risk, rapid expansion whilst providing a relatively immediate stream of profit from each market, in contrast to the current situation with operations in America. Additionally such a model could be supported from the UK, removing the need for ‘in country’ support teams currently required by other markets. There is a further potential benefit in that a franchise system could act as a stepping-stone in developing implant markets into full retail participation. In such an application, the implant could create a foothold upon which brand equity can be developed that could be further leveraged through a franchised retail model.

3. Objectives of the study

This dissertation will combine deductive and inductive research to provide recommendations as to whether the BTC model is 'franchisable' and if so which international market currently offers BRI the greatest opportunity to test the system. It begins by reviewing the literature and empirical views regarding key influences on the franchise decision as well as building a picture of the factors contributing to success.

The second part builds on a short piece of desktop research to provide, a rigorous quantitative analysis of the opportunities for BRI provided by the markets that comprise the Gulf Co-operation Council (GCC)[5] within the Middle East. Since conception, BRI has been bombarded with a huge number of invitations to partner with organisations from this region and the volume of these requests warranted a desktop investigation. This exercise highlighted that the region; featured highly in the annual results of a number notable and successful 'Western' retail franchisors (both in terms of growth and volume); was experiencing exponential growth in retail property development; was populated with a number of highly capable master franchisees; and was absent of any significant competition in the 'Boots space'. This validated the need for a 'deeper dive' and hence the second area of this study considers the opportunity for piloting a Boots franchise in the GCC.

Therefore, the empirical objectives of this study are summarised as follows:

Is the BTC model 'franchisable' and how would TBG benefit through BRI developing a successful franchise system?

Do the GCC markets currently provide BRI with an appropriate opportunity to develop and test a franchise system?

[5] The six countries currently comprising the GCC are Kuwait, The Kingdom of Saudi Arabia (KSA), The United Arab Emirates (UAE), Bahrain, Qatar and the Sultanate of Oman (Oman).

4. Dissertation structure

The dissertation is organised through a further 4 chapters, following this introduction:

Chapter 2 **Literature review**

The literature review provides a background to franchising and its variant forms. It lays out the key factors that contribute to the decision to franchise along with its risks and benefits. The final part of this section develops a number of hypotheses (tested within the research methodology) for the key factors important in successful international franchising based on a number of the literature posits researched as part of this review.

Chapter 3 **Methodology**

The methodology chapter outlines the research strategy adopted in answering the two empirical objectives of this work. It explains how the investigation utilises both deductive and inductive approaches in the collection, triangulation and analysis of both qualitative and quantitative data in arriving at the final recommendations.

Chapter 4 **Results and discussion**

The methodology utilises a progressive approach where one step informs the next and hence this chapter provides the results of each step along with an associated discussion. These results and discussions are presented for each research objective in turn before being used to build a financial model as a result of the insights derived.

Chapter 5 **Recommendations and conclusions**

The final chapter provides the recommendations from the research for each of the two empirical objectives. Each recommendation is preceded by a short summary drawing together the supporting evidence gathered through the earlier chapters. The final section provides an update of what has occurred as a result of this research.

5. Summary

This chapter has illustrated the rationale for investigating franchising as a route to international retail participation for TBG through the BRI business. It has also described how the recent upturn in global performance has facilitated a new focus on sources of growth, whilst noting that the success of the American pilot is critical if BRI is to continue its journey to profitability. In highlighting the importance of this pilot it has indicated that BRI's resources are already stretched raising the important challenge of whether striving for further growth is akin to the summit fever experienced by Everest mountaineers as they push themselves to the limit and beyond, whilst climbing in the Death Zone.

Chapter 2

Literature review

1. Prelude

This chapter reviews the literature relating to franchising. It provides some background to the advent of this business form and explains how definitions of franchising have become blurred as a result of its wider application, spawning a number of attempts at typological simplification over the last half century.

The benefits from, and reasons for considering franchising are laid out, along with a number of academic and empirical challenges highlighting that adopting this form of business requires careful consideration of the trade offs and alternatives.

This is followed by the assembly of a number of hypotheses relating to the critical success factors (CSFs) for franchise systems, which are drawn from the literature views gathered during this review. These hypotheses highlight the criticality of franchisee selection and therefore include a section summarising the views offered in this area that are particularly relevant to a potential franchisor like Boots.

2. Franchising – the term and typologies

The basic idea of franchising has been around since the Middle Ages (Henderson, 1967, p239), when franchises were granted to tax/tithe collectors (Purvin 1994) and since these times it has evolved to take on a much boarder meaning. Indeed there are a number of definitions available depending on the context of the franchise. This is illustrated by the small list offered by Price (1997, p3); it has been used in relation to the broadcasting of television programmes, the operation of airline or rail routes, the supply of utilities, the use of cartoon characters on products and the use of training packages.

The term "franchise" originates from the French word meaning to be free from servitude (Lusch et al, 1993) and the increased breadth of its present usage has contributed to much of the confusion regarding its meaning. Hence it is important that anybody unfamiliar with the term can gain a point of reference upon which to build understanding and with this in mind there is value in browsing the following simple definition:

> '*A business established or operated under an authorization to sell or distribute a company's goods or services in a particular area'*.
>
> (http://www.thefreedictionary.com)

This concept can be used to understand how the term has been used to describe a wide variety of business relationships, which often involve the owner of an asset (e.g. a trademark or brand), or *franchisor*, 'licensing' this asset for use by another party, the *franchisee*, in exchange for payment, usually in the form of a recurring royalty fee. The synonymous use of franchising and licensing agreements has been suggested as a further reason for some of the confusion and common misunderstanding associated with the application of franchising as a business model (Mendelsohn, 1992, p6).

The proliferation of franchising from the 1950's onwards, when it became the most rapidly growing form of business organisation (Oxenfeldt and Thompson, 1968), lead to the creation of a number of franchise typologies. Vaughn, for example, suggested that there were four types of franchise (1979);

The Manufacturer-Wholesale Franchise – where the manufacturer grants the right for wholesale distribution of the product(s).

The Manufacturer-Retailer Franchise – where the manufacturer grants retailer(s) the right to sell the product(s) to the final consumer.

The Wholesaler-Retailer Franchise – where the wholesaler grants retailer(s) the right to trade under a certain name.

The Retailer-Retailer Franchise – where one retailer grants another retailer the right to trade under the same name.

Pintel and Diamond (1991) went on to distinguish a further classification of ten forms of franchising relationship; territorial, operating, mobile, distributorship, co-ownership, co-management, leasing, licensing, manufacturing and service. However the most widely accepted typology has evolved through a dichotomy that distinguishes between those franchises that focus on product and those that focus on format (Combs & Castrogiovanni, 1994; Kostecka, 1986). Hence Vaughn's first three types are subdivisions of *product franchising* and his last one forms the basis for what is more often termed *business format franchising*[6].

Product franchising is best illustrated today through the global plethora of franchised car dealerships. Here the franchisor is able to provide the franchisee with products and training to which the franchisee can add their brand and financial resources e.g. Reg Vardy in the UK.

Business format franchising differs by focusing on the preparation and delivery of the service rather than the just product. It has developed out of recognition of the benefits of standardisation associated with consistent delivery in sectors where customers value a consistent standard of quality e.g. hotels and restaurants. Here the franchisor provides the franchisee with explicit and often mandatory guidance on how to operate the service so that delivery to the customer is always to the same high standard. The franchisee is then successful because customers, whether regular or transient, visit their premises knowing that they will get the same standards whether they are in their home town or anywhere in the world, e.g. Starbucks and MacDonald's.

There are also a number of other terms that are regularly used in the business context. *Master franchising* relates to the presence of an intermediate level of management between the franchisor and the individual franchised unit, which may (*area franchising*), or may not (*sub-franchising*) be solely operated by the master franchisee. *Retro franchising* (or *refranchising*) occurs where company-owned outlets are transformed into franchised outlets as a method of refinancing or restructuring a company (Seid 1992), e.g. the franchising of the rail network in the UK under the auspices of the Strategic Rail Authority. *Fractional franchising* is used to describe the activity of listing a franchised product in the assortment within an established business, e.g. a franchise store within a department store or grocer. *Upstream franchising* occurs when relationship contracts are awarded to suppliers rather than retailers, e.g. the petroleum industry. Finally, *Ownership*

[6] Business format franchising has in turn tended to be categorised by the size of the initial investment into three types; *job franchise* (where the franchisor creates a job for a self-employed individual), *business franchise* (normally a larger investment involving business premises and additional staff) and *investment franchise* (relatively large investment such as a chain or significant premises such as a hotel; Macmillan, 1996).

franchising, where the franchisor owns a stake of the franchisee's business[7], e.g. Starbucks (Winsor, 1998).

3. Motivating factors in the franchise decision

i. *Why franchise the business concept?*

The decision about whether or not to franchise has received a considerable degree of attention throughout academic literature. Price (1997) offers a classification of the motivating factors that is useful to draw published views together. He advocates that the reasons purported to prompt businesses to investigate franchising, over and above the rationale for creating inter-organisational relationships in general, can be separated into three areas: resource scarcity; agency theory; and risk spreading.

a. *Resource scarcity*

Relationships are often developed between different organisations as a means to obtain resources. Franchising can be route to formalise such relationships either through a franchisor seeking access to the resources owned by, or available to, a franchisee as well as, through a franchisee seeking to gain access to a franchisor's competencies or trademarks. Although, many of the explanations for franchising decisions in this area relate to the reasons from the franchisor's point of view. The thesis that has become known as the 'ownership redirection thesis' is rooted in this area of resource constraints. Oxenfeldt and Kelly (1968) posited that franchisors only chose to franchise in order to attract capital and that once the business has grown they will seek to buy back all but the marginal outlets. This argument is based on the assumption that raising capital in this way is more efficient than selling shares in the company and there are examples of empirical research, which support this thesis (Hunt, 1973; Manolis *et al*, 1995). However there are also researchers who offer opposing views.

[7] This may occur where the franchisor funds the franchisee in return for a stake in the business or where the franchisor buys into the franchisee's business after a period of success.

Rubin (1978) led the dissenting voices with his view raising share capital provides a diversified company with a superior alternative because diversified investors require lower returns than the less diversified franchisee. Lafontaine (1992) offered further evidence that some companies don't use franchising as a route for immediate capital generation through her observation that some franchisors finance their franchisees to increase their proportion of franchised outlets. Kaufmann *et al* (2000) offer a potential explanation for why firms may chose to do this in their observation that the optimal mix of franchised and company owned outlets may depend on whether measures of accounting value (AV, e.g. net income and earnings per share) or economic value (EV, e.g. net operating profit after tax and operating return on assets) are used to manage and monitor performance[8]. Hence it is fair to say that there is inconclusive evidence as to whether resource scarcity, in particular financial resources, provides a reason for the decision to franchise.

b. *Agency theory*

The arguments concerning agency theory, on the other hand, have much wider acceptance. Fama and Jensen (1983) assert that 'an organizational form survives in an activity when the costs and benefits of its residual claims and approaches it provides in controlling agency problems continue with available production technology to allow the organization to deliver products at lower prices than other organizational forms'. Thus in their view organisational forms are influenced by the desire to reduce agency costs and control agency problems. Michael (1996), illustrates how franchising is able to do this summarising it as 'a way to allocate decisions within the fanchise system between the franchisor and the franchisee in order to promote efficiency and provide incentives'. Brickley and Dark (1987) add their perspective through reference to the position of franchising as one extreme of the managerial compensation continuum. They see it providing the franchisee with an incentive-based compensation as franchisees are encouraged to influence their returns by eliminating the activities, which generate agency costs within company chains. Close monitoring of these franchisee behaviours can result

[8] For EV maximising retailers, the cost of capital tied up in company owned outlets is charged against net income. Hence franchising becomes attractive even when sufficient capital is available to open company-owned units.

in additional franchisor benefits in the event that their own employees successfully replicate these insights.

However there are again, opposing views to agency theory being a solid reason for franchising. The economists (Kaufman *et al*, 2000) illustrate this in describing the impact of agency costs on the franchising decision in a firm focused on AV measures. They assert that such firms would not franchise unless, their agency costs caused them to generate lower net operating profits than they would from a franchise alternative. They further suggest that as such situations rarely occur the decision for an AV maximising retailer (such as TBG) to franchise would only be the result of a lack of any alternative capital source. This is supported by Lafontaine's observation (1992) that as the issues relating to agency costs are well understood it would be reasonable to expect that investors would demand higher returns as a result and this in itself could swing the balance towards franchising being more about a superior route to raise capital than it is necessarily about managing agency costs.

A further opposing, but nonetheless valid, point is raised by Combs and Castrogiovanni (1994). They note that whilst franchising offers a route to reduce the costs involved with monitoring 'inhouse' employees, it also introduces costs of monitoring the franchisees. This is especially important where a firm is keen to maintain the integrity of its brand and protect equity that it has spent many years building (e.g. the Boots Brand).

c. *Risk spreading*

Price (1997) maintains that risk spreading relates to the view that franchisors are risk averse and seek to retain control over more profitable units, while shedding the riskier locations through a franchise system. Dev and Brown (1990) have provided empirical evidence of this activity being prevalent in the hotel industry with firms seeking to own hotels in low-risk locations but offering franchises in high risk regions. However, Michael (1996) offers a counter to this in his model of the franchise decision by asserting that 'Franchising will be chosen less frequently relative to other organisational forms, the higher the level of business risk in a given industry'. This position is derived from the view that franchisees will demand greater compensation from a risky location, which could mean that franchising becomes more costly.

d. Customer mobility

Michael's model (1996) also adds to Price's earlier classification of the reasons for franchising. It offers the view that the decision may also be based upon the ever increasing degrees of customer mobility. This is especially important in terms of international retailing as customers who purchase in several local markets are exposed to higher levels of uncertainty regarding product or service quality. Business format franchising gives customers some salvation from this uncertainty and it has been suggested that it has more value and is therefore more common in industries where customers regularly purchase across markets.

e. Summary of benefits and disadvantages

In addition to these four areas there are a number of other benefits that support the use of a franchise model. However these benefits must be traded off with a similar list of downsides before a firm embarks on establishing a franchise system. Figure 2 has been adapted from Price's review (1997) to provide a summary of both sides of the franchise coin.

Benefits of franchising

- Access to resources; capital, local market knowledge, innovation.
- Reduced agency costs; highly motivated and committed franchisees that share profits.
- Reduced risk, especially in untested international markets.
- Improved security as outlets are less likely to be targeted by xenophobic activities if locals own them.
- Consistent, broader and faster brand dissemination, driving further cost reductions through scale.
- Reduced organisational support costs – smaller head office requirement.
- Positive cash flow – often from day 1.
- Enhanced chances of success.
- A solution to market entry barriers e.g. requirement for part ownership by a native.

Disadvantages of franchising

- Difficulties in exercising tight control over franchisee and getting total compliance.
- Franchisees may create damage to the brand leading to difficulties in the domestic market.
- Franchise agreements can be lengthy and may present costly problems for a franchisor wishing to exit them.
- Changes in corporate strategy can take longer to implement.
- Franchisee relationships and their management may require changes to organisational culture.
- Franchisee may not be honest with their declarations of business activity.
- Franchisee recruitment may require compromise leading to relationship difficulties.
- Franchisors may lose key personnel.

Figure 2. The benefits and disadvantages of franchising for franchisors

ii. Business model CSFs

The previous discussion illustrates the benefits and downsides that need to be considered in making the franchise decision. However any trade offs must also consider how the format or brand under consideration stacks up against these factors, which are argued to be critical to the success of any franchise system. My observations through this literature review have led me to build some hypotheses for CSFs organised in two categories, firstly aspects of the *business model* being franchised and secondly aspects of the *markets* to launch the franchise in.

A number of these may well appear obvious but they are nonetheless critical and warrant consideration, e.g. the importance of the profitability of the business being franchised. Franchisees will be investing resources in the business and it will need to be capable of delivering sustainable returns on their investment. These returns should be founded on a source of competitive advantage that is not easily imitable and this is why so many successful franchises are built around well-known brand names; whilst competitors can copy outlet operations they cannot copy the brand name and its heritage.

CSF (H)[9] *A1 – The franchise model must be based on a proven, profitable and non-imitable brand or business proposition.*

Franchising is particularly prevalent in businesses that can be easily and consistently replicated. Hence it is important that the business can be systemised so that it can be easily taught to the franchisees and their employees.

CSF (H) A2 – The franchise model must be systemisable and easily translated into simple formats that can be taught to franchisees.

Franchisee selection and compliance are recurring themes throughout the franchising literature. Bradach (1998) highlights how a number of US franchisors place a huge emphasis on getting this right, not least because exiting a poorly selected franchisee can be hugely problematic. Shane (1996) argues that firms who successfully expand internationally through franchising possess a superior capability to reduce the opportunism, which 'is always incentivised between two independent entities in a market setting,' (Williamson, 1985). Such capability is asserted to manifest through the abilities

[9] (H) indicates the CSF is 'hypothetical' to distinguish it from the refined version (R) refered to in the latter chapters of this report

of providing franchisees with an incentive to refrain from opportunism and dosely monitoring any such occurrences. Shane suggests that an ex-ante bond, such as a high franchise fee, which is forfeited in the event of opportunism, provides an incentive to avoid opportunistic behaviour and that in support of this the franchisor should install monitoring procedures, which inspect franchisee records and facilities to ensure compliance. However whilst doing so franchisors must ensure such procedures don't costs as much as the agency costs that would be associated with an in house operation.

CSF (H) A3 – The franchisor must develop and commit to following a recruitment process that ensures the optimal choice of franchisee.

CSF (H) A4 – The franchisor must install and enforce a monitoring system to ensure compliance with the policy described in their operating manual.

Whilst a monitoring system is vital there is evidence to suggest that a franchise system will benefit from the franchisee having licence to establish their operational management processes. Shane and Spell (1998) suggest that scarce franchisor resources should be devoted to growing the franchise system rather than seeking to control franchisee activities relating to activities such as site selection and training. I can agree with sentiment of this point however I have amended it in creating an associated hypothesis because I feel that this position should be revised according to level of trust that the franchisor has in the franchisee's ability to make the right decisions in these areas.

CSF (H) A5 – The franchisor must support the development of the franchisee's operational capability and then step back to allow them to run their franchise in accordance with the franchisor's policy.

iii. Market CSFs

Again some of the factors relating to characteristics of the market may appear obvious but can often be overlooked. The following hypotheses for CSFs relating to market selection build on the ideas of Mendelsohn and Acheson, offered by Macmillan (1996). The first one is based on the foundation of economics, i.e. supply and demand, in that the market must exhibit a latent or actual demand that can be met through the franchise system. In addition to this it would appear logical, from Michael's model (1996), to suggest that markets characterised by existing awareness for the brand to be franchised will be more successful at the outset. This awareness would reduce the initial launch expenses and also present a more attractive proposition to prospective franchisees looking to benefit from instant sales (Oller, 2002).

CSF (H) B1 – The market must be characterised by existing brand awareness and growth in the sectors which will be served by the franchise system.

Following on from the issues relating to franchisee selection above, consideration must be given to whether the right calibre of franchisees are available in the market.

CSF (H) B2 – The market can provide a pool of cash rich, capable franchisees with the ability to develop the skills required to operate the franchise

Finally, I have often heard colleagues in the Boots property division say that there are three things that must be right for successful retailing, namely location, location and location. Whilst I don't totally agree, the point they make is valid and one worth considering when looking at a new market, especially in this case where a test market for a new franchise system is being considered.

CSF (H) B3 – The market can provide franchisees with a selection of suitable real estate options, which aren't prohibitive to outlet profitability.

iv. Franchisee selection CSFs

Having established that there are benefits to be gained through franchising, the above hypotheses for CSFs indicate the importance of the franchisor's approach to selecting the franchisee(s). Literature provides some theses in this area that are pertinent to this study.

Macmillan (1996) makes the pragmatic observation that in practice, this process often involves some degree of compromise, despite the fact that much of the literature insists it is a mistake to accept a franchisee unless they match the requirements in every respect. He notes that a critical failing of the franchisor is in drawing up an accurate skills profile for the franchisee and that this failure leads to poor screening leading to selections based on the availability of financial resources rather than competence.

CSF (H) C1 – Draw up a franchisee skills and attributes profile and apply this rigorously when screening franchisees.

Jambulingham and Nevin (1999) provide some empirical evidence for the criteria that should be considered by franchisors in selecting franchisees. They suggest that franchisee's attitudes to business (particularly through the dimensions of commitment and innovativeness) are critical, in addition to looking for prior experience, management skills and evidence of calculated risk taking (rather than all out gambling!).

CSF (H) C2 – Franchisee should possess a positive and committed attitude to the business; show evidence of innovation and calculated risk taking; and demonstrate competence in brand and business management.

In many ways the most important element of the franchise system is the relationship between the franchisor and franchisee. Hence it is also vital for the franchisor to select franchisees with whom they have 'the right chemistry'.

CSF (H) C3 – Chose franchisees with whom there is the 'right chemistry'.

One outstanding problem for franchisors is in attracting franchisees to assess against these criteria. Macmillan suggests that exhibitions are effective but these are public events that are inappropriate if a firm is seeking a 'quiet' entry to obtain a first mover advantage. Walker and Etzel (1973) have observed that much international expansion occurs in response to inquiries from potential franchisees and this may well be due to this desire to avoid early publicity. Therefore it is important that franchisors not only seek to apply the appropriate criteria when selecting franchisees but also invest in considering how they market what is essentially a product they are seeking to sell, through the selection process.

CSF (H) C4 – The selection process must be based around the sale of the franchise system to the franchisees.

v. International expansion through franchising

This final section draws together other notable areas relating to international franchising and offers further hypotheses for additional CSFs that must be considered in the decision to franchise outside of domestic markets.

Aydin and Kacker (1990) suggest that overseas expansion through franchising is either the result of domestic market saturation, i.e. a route to alternate sources of growth, or a desire to take advantage of a foreign market with great potential. These views open up some further areas for consideration when linked with other posits in the literature. Garg et al (2005) have shown that the driver behind the strategy can be related to the choice of the structure of the franchise system. They have shown that franchisors with high growth aims tend to adopt a multi-unit approach based on area development rather than single unit franchising. If this is considered alongside a further observation that franchisors prefer to grow by establishing a franchise and saturating a geographical area with it before expanding to a new location (Martin, 1988), one can formulate an additional hypothesis relating to this investigation.

> *CSF (H) D1 – Franchisors with high growth aims wishing to expand outside their domestic market through franchising should do so through saturation of the area via a system utilising multi-unit agreements for the area.*

The earlier section on CSFs highlighted Shane's view that a system for monitoring and ensuring franchise compliance was important when expanding internationally. In addition to this, Huszagh et al (1992) identified that proficiency in procedures for site selection and store design are also important drivers in the decision to franchise overseas.

> *CSF (H) D2 – Franchisors seeking successful overseas retail expansion through franchising need to be skilled in site selection and store design procedures.*

4. Summary

This chapter has provided a review of the literature relating to franchising and highlighted the increasingly broad applications of the concept of franchising, illustrating why there is no clear-cut literature definition for the term.

It has provided a balanced review of the potential reasons why a firm may chose franchising as a business model as well as the benefits and potential drawbacks which need to be traded off in making this decision.

The review has facilitated and informed the synthesis of a number of hypotheses (drawn together below) for the CSFs for successful international franchising which will be validated within the approach of this research.

CSF (H) A1 – The franchise model must be based on a proven, profitable and non-imitable brand or business proposition.

CSF (H) A2 – The franchise model must be systemisable and easily translated into simple formats that can be taught to franchisees.

CSF (H) A3 – The franchisor must develop and commit to following a recruitment process that ensures the optimal choice of franchisee.

CSF (H) A4 – The franchisor must install and enforce a monitoring system to ensure compliance with the policy described in their operating manual.

CSF (H) A5 – The franchisor must support the development of the franchisees operational capability and then step back to allow them to run their franchise in accordance with the franchisor's policy.

CSF (H) B1 – The market must be characterised by existing brand awareness and growth in the sectors which will be served by the franchise system.

CSF (H) B2 – The market can provide a pool of cash rich, capable franchisees with the ability to develop the skills required to operate the franchise.

CSF (H) B3 – The market can provide franchisees with a selection of suitable real estate options, which aren't prohibitive to outlet profitability.

CSF (H) C1 – Draw up a franchisee skills and attributes profile and apply this rigorously when screening franchisees.

CSF (H) C2 – Franchisee should possess a positive and committed attitude to the business; show evidence of innovation and calculated risk taking; and demonstrate competence in brand and business management.

CSF (H) C3 – Chose franchisees with whom there is the 'right chemistry'.

CSF (H) C4 – The selection process must be based around the sale of the franchise system to the franchisees.

CSF (H) D1 – Franchisors with high growth aims wishing to expand outside their domestic market through franchising should do so through saturation of the area via a system utilising multi-unit agreements for the area.

CSF (H) D2 – Franchisors seeking successful overseas retail expansion through franchising need to be skilled in site selection and store design procedures.

Chapter 3

Methodology

1. Prelude

This chapter describes the approach and methodology employed in undertaking this research. This methodology utilises both deductive (theory testing) and inductive (theory building) approaches and as such the philosophy for this research draws on both positivism and interpretivism (Saunders et al, 2003).

The research and analysis has been undertaken over a period of 6 months during 2005 as a result of the conducive climate within BRI and the authors determination to complete a research project of immediate business value whilst providing a basis for the dissertation required for the MBA degree. In many cases the data gathered is protected by confidentiality agreements and as a result many of the individuals and organisations that have provided much of the data remain anonymous.

The data collection and research includes both qualitative and quantitative methods and the reasons for their use are explained, together with their limitations, alongside each of the elements within the research strategy.

2. Research strategy

The introduction has detailed the two main questions at the heart of this piece of work and the research strategy has been developed around answering these questions (Saunders et al, 2003).

i. Methodology for objective 1

The first objective was to establish whether the BTC retail model is 'franchisable' and the benefits that TBG stand to gain through the addition of a franchising option to the

BRI model. The approach developed to answering this question resulted from breaking the question down into distinct areas of focus related to benefits, risks and their implications for Boots;

- Why do companies choose to employ a franchising route to support international growth?
- What are the CSFs for international franchising?
- What are the implications of these two questions for TBG, i.e. the likelihood of successfully franchising BTC stores overseas; and how does the risk versus benefit analysis support or prohibit a strategy of international expansion through franchising?

Two qualitative routes were taken in answering the initial questions before looking at their implications for Boots. The first involved a literature review to source the theoretical, academic and consultative views relating to franchising. This review (Chapter 2) facilitated the development of a series of hypotheses used as the basis for questions (Appendix 1) asked during interviews with senior managers from a selection of companies who successfully employ franchising as part of their international retail strategies. A short list of target companies was prepared following a review of non-competing companies who have experienced successes through franchising. Five of the companies approached agreed to take part in this research (Table 2) and the subsequent semi-structured interviews lasted approximately 90 minutes.

The information gathered through the literature review and tested in the interviews was assimilated into a set of criteria for successful international franchising. In addition to these criteria this data also facilitated the creation of a collection of common benefits and risks associated with operating franchise systems.

Company Reference[10]	**Sector and recent franchising comments from latest accounts**
Company A	Fashion; latest sales 9.1% inc. yr on yr
Company B	Food; latest revenues from franchising 20% inc. yr on yr
Company C	Fashion & toiletries; latest sales 17% inc. yr on yr
Company D	Fashion; new entrant but sales greatly exceeding original forecasts
Company E	Fashion; latest sales 16% inc. yr on yr, Middle East is largest region

Table 2. Most recent international financial results for practitioner company sample

The last part of this section of the research involved testing the characteristics and profile of the TBG against both of these data sets to confirm the validity of continuing with the research and inform the final recommendation relating to the feasibility of franchising the Boots retail brand. The approach to this step involved a direct comparison of TBG with the refined hypotheses by the author in the role of practitioner researcher (validated by 15 years of employment in the group).

The decision for this dual approach to data gathering resulted from a preference to triangulate the literature data with the experiences of contemporary practitioners and hence add to its credibility, ahead of its intended final interrogation by the notoriously risk adverse decision makers in TBG. It allowed theories extracted from literature to be corroborated and modified as described in Robson's deductive research sequence (1993) before organising the relevant insights into a set of criteria that could be applied as a test of the feasibility of creating a Boots franchise system. Data was gathered from contemporary practitioners through semi-structured interviews as it has been suggested that this approach enables the interviewer to access details of 'why' in addition to 'how' and 'what' (Saunders et al, 2003), through probing supplementary questions which are not possible though questionnaire based approaches (Sykes, 1991).

[10] The Companies supporting this research have requested anonymity and have been assigned letters to facilitate direct reference throughout the results and following discussion.

ii. Limitations of the approach to objective 1

There were however still a number of limitations associated with this technique such as subjectivity, preconceived biases (Borg, 1981), reliability (Easterby-Smith et al, 2002) and its applicability to generalisation (Bryman, 1988). This research has recognised these challenges and whilst accepting that it is not possible to overcome them all has sought to mitigate against some of them through the use of the interview data to triangulate theory (Marshall and Rossman, 1999) and the use of a consistent list of opening questions for the interviews (Appendix 1).

A further challenge associated with the collection of qualitative data comes in that its diverse nature means it doesn't lend itself to a standardised analytical approach. As a result the analysis of this data followed Tesch's strategy of discovering regularities (1990)[11] to compliment the deductive approach[12]. To support this all interview notes were written up immediately (to reduce the incidence of reflective subjectivity) and then reviewed together to establish a set of categories covered in one or more of the interviews. Having established these categories the analysis proceeded through a comparison of the data provided by each interviewee within each category.

iii. Methodology for objective 2

The second research objective was to establish whether the GCC markets provided BRI with an appropriate opportunity to develop and test a franchise system. These markets were initially identified through a somewhat subjective and intuitive process. Thus it was imperative that a little more rigour was included in the design of this part of the research.

This research also assumes that the system will be supplied from two sources; BRI providing Boots branded or exclusive inventory, and the franchisee sourcing other inventory[13] themselves. Hence the inclusion of inputs relating to the range of inventory that a franchisee could source in the region (e.g. size of store, type of locations, sales

[11] Tesch (1990) groups strategies for analysing qualitative data into four categories; understanding the characteristics of language, discovering regularities, comprehending the meaning of text or action, and reflection.

[12] The first two are associated with analytical strategies that commence deductively and the latter two those that commence inductively (Saunders et al, 2003).

[13] The lower margins on proprietary branded FMCG and commodities products make it value destroying to ship them from the UK.

intensities) represented a critical element of the design of the franchise system. As a result the methodology depicted below (figure 3) includes inviting candidate franchisees to prepare business proposals to inform the design of the system[14].

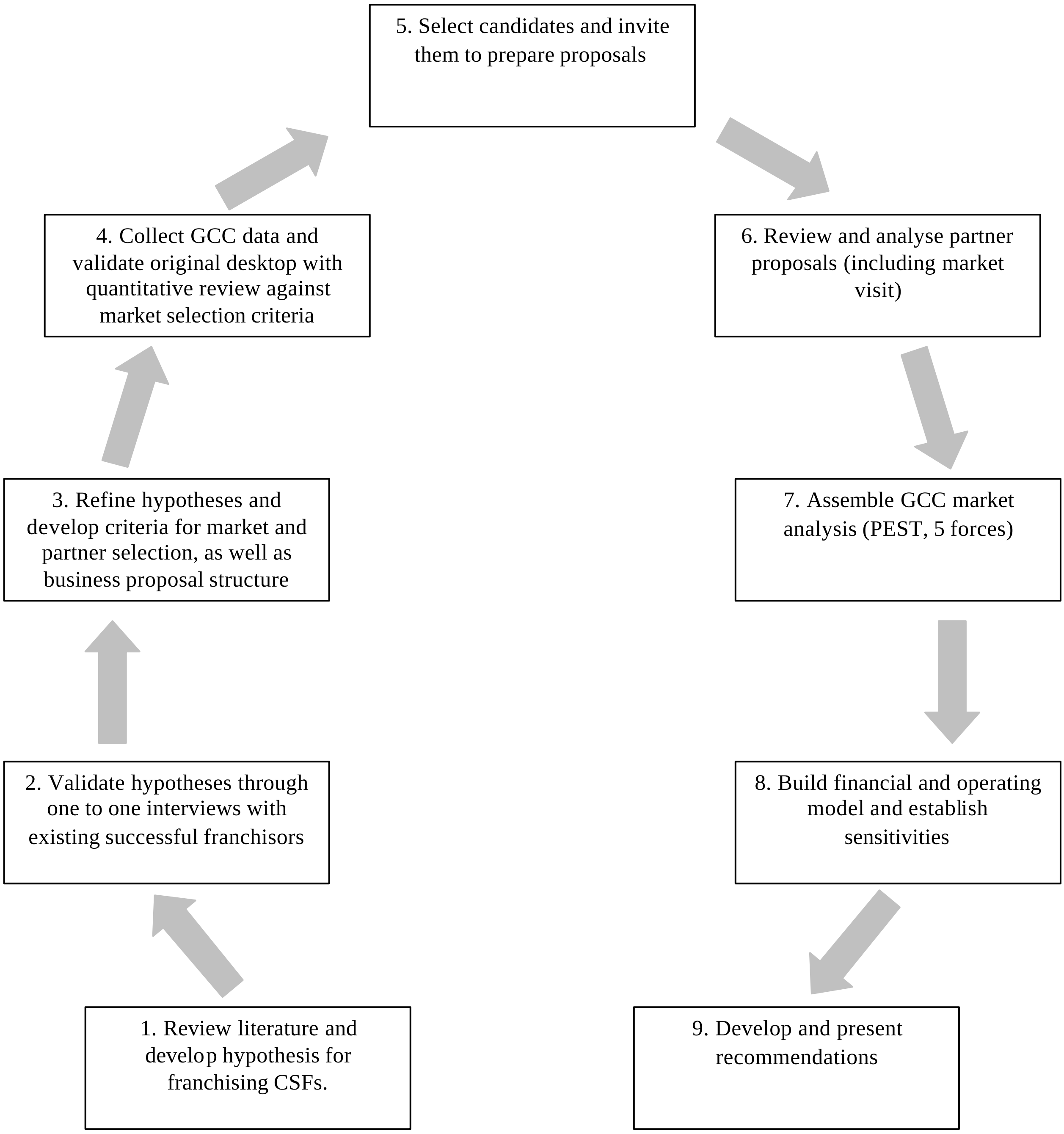

Figure 3. Flow diagram of methodology adopted for second research objective

[14] This approach provided the additional benefits, highlighted by the interviews, of gaining insights into the capabilities and behaviours of potential franchisees, as well as a source of triangulation for quantitative data collected remotely from the UK in step 4.

The first step occurred in parallel with the research related to the first objective and produced test criteria to assess the opportunity presented through the GCC markets. The inductive approach to deriving this list involved building a set of theoretical criteria to apply to the markets reflecting the elements important to the development of a Boots franchise system, utilising literature theses. These were then validated and modified through the second step that utilised the opportunity presented by the contemporary practitioner interviews[15].

The third step involved reviewing the content of the interviews in order to create three sets of information, firstly the refined criteria against which to test the GCC as a suitable test market, secondly the ideal attributes which would be used to shortlist the extensive list of speculative enquiries received by BRI and thirdly the structure against which, willing shortlisted candidates would be invited to prepare business proposals (Appendix 3). In each case the approach followed the previously explained strategy of discovering regularities in the analysis of qualitative data collected from the literature review and interviews.

These steps were followed by a quantitative review of the GCC market that involved collating data from a number of reputable sources such as AC Nielson, as well as other publicly available on-line sources. This step provided some robust insights, which supported the validity of requesting business proposals from potential GCC franchisees. Hence step 5 involved short-listing franchisee candidates by assessment aginst the criteria developed in step 3 to derive a list of 12 potential candidates who were invited to prepare business proposals[16] aligned with the structure also developed in this step (Appendix 2).

Step 6 involved an analysis of the completed proposals followed by the selection of two candidates to visit in the market. This visit validated the claims made within the business proposals and provided personal observations of the opportunities presented by the GCC

[15] The early development of this research strategy alongside the approach for the first objective allowed the outline of the interviews with external contemporary practitioners to include questions relating to both objectives of this research (Appendix 1).

[16] In order to ensure that this exercise remained entirely ethical, all of the candidates were informed; that a number of parties had been invited to prepare proposals, and that there was no guarantee that any one of these would be invited to become a franchisee as a result of these submissions, which were clearly stated as contributions to a feasibility analysis by Boots concerning franchising in the region. In addition to this it was made clear that any further correspondence including further input data such as assumptions on operating configuration and product margin would only be undertaken once a signed confidentiality agreement was in place (Appendix 3).

market. This review was used to inform both a full GCC market analysis and the development of an operating and financial model for the proposed franchise system. Once assembled this model was subjected to a sensitivity analysis to establish the key variables and test the feasibility of the profitability of the entire enterprise. The insights from these two penultimate steps were then drawn together with the rest of the research to prepare the final recommendations.

iv. Limitations of the approach to objective 2

Despite the application of a methodology that again sought to remove bias and provide points of triangulation, the approach taken for the second objective was not without limitation. It has already been noted that the initial selection of candidates was limited and this may have meant that the breadth of options portrayed within the business proposals were limited. In addition to this financial constraints relating to the market visit meant that only two candidates were able to provide in depth market perspectives, whereas had all five been able to host visits one would have expected the insights gathered to have offered a far richer picture of the market.

A further potential limitation of this approach lies in the fact that the prospective candidates were drawn from the database of speculative enquires received in BRI since 1996. This undoubtedly meant that there were some capable potential franchisees who were not involved, however the absence of any additional recommendations for candidates from the region during the interviews supports an assumption that the net was cast sufficiently wide for the purposes of this research.

3. Summary

This chapter has outlined the research philosophy and investigative strategy employed in undertaking this dissertation. It has highlighted how it has been necessary to utilise a number of deductive and inductive approaches in answering the two objectives. Whilst it has presented the strategies for each objective separately it has demonstrated how planning the methodologies for both at an early stage maximised the opportunity for gathering data concerning both objectives from external practitioners.

It has also recognised the limitations of the approaches and shown how the use of multiple data sources, including contemporary practitioners and potential franchisees, has provided points of triangulation to validate the insights and support credible final recommendations.

Chapter 4

Results & discussion

1. Prelude

This chapter details the results of the qualitative and quantitative elements of the approaches described in the previous chapter on methodology. The steps comprising these approaches were sequenced to enable each one to inform the next and hence each set of results is followed with a discussion informing the next.

The qualitative results of the semi-structured interviews are presented in two sections relating to the two research questions. These describe how the initial hypotheses developed earlier were validated or refined to inform the later steps in this research.

This is followed by a presentation and analysis of quantitative data. GCC market data gathered from the UK is analysed and tested against the criteria refined as part of the qualitative research. This illustrates the value in approaching potential franchisees to support the investigation through the submission of business proposals.

These proposals are compared and summarised against the criteria for partner selection refined through the qualitative section. The insights gathered through the proposals and a subsequent validation visit to the market are then drawn to together in an environmental analysis which validates the opportunities and assumptions developed by the candidate franchisee proposals.

2. Qualitative analysis of semi-structured interviews

The content of the interviews covered elements of both of the research questions for this report and the results are presented following an analysis to discover regularities as described by Tesch (1990).

i. Results relating to research question 1

The first research question involved understanding the reasons why companies adopt franchising as a route for expansion as well as the associated CSFs, risks and benefits of the decision. The literature posits and other hypotheses developed above (Chapter 2) were used as the basis for semi-structured interviews, which allowed the participating companies to validate or refute these arguments.

a. Why do companies chose to franchise?

The franchise literature suggests that firms franchise as a route to the benefits of overcoming issues relating to resource scarcity, agency theory, risk and customer mobility. However the interviewee responses (see Appendix 4) indicated that the reasons behind the decision were actually primarily focused around risk spreading and access to cheaper capital. Some interviewees also mentioned the route to rapid growth and one raised the desire to access resources necessary to overcome barriers to entry. It was also noteworthy that none of the respondents made any mention of the issues relating to agency theory even when the interviewer suggested this.

b. What are the associated risks and CSFs?

Responses to questions concerning the risks and related critical factors for success showed a closer degree of congruence with the hypotheses described in chapter 2 (Table 3). All the interviewees agreed that the greatest risks were brand related. Control over franchisee brand management is exerted through a prescriptive operating manual (supporting *CSF (H) A4*) that consists of both mandatory requirements and operational guidance. Each company had invested time in developing their manual and ensured that their contractual agreements clearly stated that failure to meet the mandatory requirements could result in an immediate withdrawal of the permission to trade under the brand name or trademark. The discussions in this area also raised the importance of providing full training before opening the business as well as regular compliance checks and business reviews (supporting the monitoring element of *CSF (H) A4*), managed by a domestically based franchise management team.

Hypothesis validated or refuted	Company A	Company B	Company C	Company D	Company E
CSF (H) A1	Validated	Validated	Validated	Validated	Validated
CSF (H) A2	Validated	Validated	Validated	Validated	Validated
CSF (H) A3	Validated	Validated	Validated	Validated	Validated
CSF (H) A4	Validated	Validated	Validated	Validated	Validated
CSF (H) A5	Partial	Partial	Validated	Validated	Partial
CSF (H) D1	Validated	Validated	Validated	Validated	Validated

Table 3. Interviewee responses relating to hypothetical business model CSF's

The interviews also discussed the type of agreements and the importance of selecting the right franchisees. All of the companies tend to use a master or area franchise agreement to develop the business across a market or region (supporting *CSF (H) D1*) and as a result invest a significant amount of resource in selecting partners who fit a certain profile (supporting *CSF (H) A3*).

Contract structure was another common theme and the employment of a semi-structured approach allowed the interviews to go 'off plan' and discuss this area in more detail. These conversations highlighted that master franchisees tend to require longer agreement terms because their investment levels are higher and associated pay back periods are longer.

The interviewees held different views about the length of the agreements. Company B preferred longer agreements as they saw them demonstrating franchisee commitment, whilst the others accepted longer terms which provisioned for renegotiation after periods of 5 to 10 years. One innovative option was provided through company C that has agreements at the level of individual outlets allowing them to enforce closure of what they referred to as 'pups' without the requirement to renegotiate or cancel the entire agreement.

There were also a number of other key points discussed concerning contracts and these are summarised below.

1. The contract should follow a recognised format and Eversheds are the UK experts in preparing franchise contracts.
2. The contract should be governed under the law of England and Wales.
3. The contract should have a maximum term of 20 years (preferably much shorter) and include a break and renewal clause.
4. The contract should include options for the purchase of equity in the enterprise based on a predetermined and agreed purchase price formula.
5. The revenue streams should be clearly stated, with detailed payment schedules.
6. The revenue streams should be derived from some or all of the options from; franchise fee, margin on goods supplied, fee for the provision of store design drawings and royalty on retail sales (TESP[17]).
7. The contract should make provision for the franchisor to commission an independent audit to monitor the accuracy of royalty payments.
8. The contract should clearly state that the operating manual forms a material part of the contractual agreement.
9. The contract should include a 'no competition' clause preventing the franchisee from working with competing brands.

The interviewees were completely agreed on the validity of CSF *(H) A1* & *CSF (H) A2*, i.e. that ideally the franchise system should be based on a successfully proven model, which can be systemised and taught to franchisees through simple formats, often accompanying or reflecting the content of the operating manual. These discussions relating to teaching the system to the franchisees also provided some support to *CSF (H) A5* in that there was a broad agreement of the need to support the development of franchisee operational capability. However this area also highlighted differences across the companies in their approach to ongoing management as three companies stressed the

[17] TESP – Tax exclusive selling price, i.e. the retail price less any VAT.

importance of maintaining a ‘hands on’ approach, rather than stepping back, until they were satisfied with execution and trusted the franchisee to manage the brand effectively.

Hence as a result of the interviewees it is possible to refine and add to the initial hypotheses for CSFs related to the first research question, these refinements are listed below;

CSF(R[18]) A1 - The franchise model must be based on a proven, profitable and non-imitable brand or business proposition.

CSF(R) A2 - The franchise model must be systemisable and easily translated into simple formats that can be taught to franchisees.

CSF(R) A3 – The franchisor must develop and follow a recruitment process that ensures the optimal choice of franchisee.

CSF(R) A4 - The franchisor must install and enforce a monitoring system to ensure compliance with their operating manual. This manual must provide clear details, accompanied with associated franchisee training, of the mandatory and contractual requirements for the execution and management of the brand.

CSF (R) A5 – The franchisor should maintain an enhanced monitoring position until new franchisees have demonstrated a sustainable ability to deliver the required standards, then step back and allow the monitoring system and operating manual to act as tools to ensure operational compliance.

CSF(R) D1 - The franchisor should work with a single master franchisee in each international market or region.

There were also three risks highlighted in the literature, which were not validated through the interviews. The interviewees had no experiences of problems relating delays in changes to corporate strategy, losing key personnel to the franchisee organisations or problems with organisational culture, although in the latter case there were a number of suggestions that this was due to the fact that international business was a separate division with its own culture distinct from that of the domestic operation.

[18] R indicating that the CSF has been refined as a result of the empirical research

ii. Discussion of results and implications for TBG

These results show a remarkable degree of agreement across the characteristics of a franchise system, the risks in operating one and the manner in which these risks are managed. A key area of this management, not highlighted by the literature review, related to the structure of the franchise contract and the discussions in this area were particularly valuable. One might critique the consistency of the responses through a suggestion that the questions led the interviewees to offer validating responses, however the reality during the interviews was that the majority of the responses were elicited through the open questions rather than the somewhat more leading supplementary enquiries.

The refined CSF's provide a valuable contribution to the direction of this research when used to test the viability of a Boots franchise system. Firstly, the Boots brand, whilst not tested in a franchised format, does meet the conditions of *CSF(R) A1*, i.e. it is proven, profitable and inimitable as evidenced by the UK and Thailand businesses. Secondly, the fact that the UK retail offer has been successfully refined and replicated in Thailand suggests that it is possible to use systemise the business model and create a Boots franchise system, which warrants a trial in a suitable international market (supporting *CSF(R) A2)*. The last four remaining CSFs provide some insights into the critical elements that need to be in place as part of system design and implementation, i.e. a robust franchisee selection process, an understandable and prescriptive brand manual supported by comprehensive franchisee training, a quality compliance monitoring system and regional development through a master franchise agreement.

iii. Results relating to research question 2

The second research question was concerned with establishing whether the GCC markets are an appropriate place in which test a Boots franchise system. The initial approach to this question involved asking the interviewees questions relating to market and partner selection as a route to validating or disproving further hypotheses developed from the literature.

a. What characterises a successful market for a franchise system?

The literature review led to 3 hypotheses relating to market selection and the interviewees were able to provide some empirical evidence, which supported these arguments. All the interviewees agreed completely with the first hypothesis (*CSF (H) B1*) relating to the importance of existing brand awareness and whilst some had experiences of entering markets where their brands were not known they agreed that existing brand awareness makes the entry much easier.

The importance of the financial resources possessed by potential franchisees has already been highlighted above and this was endorsed during the discussions about the market selection criteria. All the franchisors agreed that the best markets are those that offer a selection of potential franchisees who all have access to both financial resources and a relational network conferring access to real estate in the prime locations. This allows the franchisor to have a stronger bargaining position than when there is one dominant potential franchisee who can lever their relational power during contract negotiations, knowing that the franchisors have little other choice if they want to enter the market (evidence for *CSF (H) B2* and *CSF (H) B3*).

In addition to the characteristics described in the hypotheses relating to franchising the interviewees also pointed out the importance of reviewing the attractiveness of the market through tools, such as a PEST or five force analysis (Porter, 1980). A noteworthy position adopted by the fashion retailers in particular was to welcome a market with a strong degree of competition as it indicated a high demand for their product. This was especially attractive for companies A & E who had experience of their global brand awareness affording them a differential advantage that allowed them to capture market share quickly in such competitive environments.

A further and prudent caution was offered during the discussion with the interviewee from company B who highlighted the challenges posed by the market specific registration requirements which had prevented them exporting to a number of markets and necessitated the development of a local manufacturing capability.

A final important point arising from the interviews in relation to market selection was the completion of a successful pilot or trial. In all cases the interviewees adopted an approach based on dipping a toe into the market through a trial and stopping to review and localise the model before embarking on a full blown rapid expansion across the market.

Therefore the refined hypotheses relating to market selection are;

CSF(R) B1 - The market should be characterised by existing brand awareness, growth or demand in the sectors that will be served by the franchise system.

CSF(R) B2 – The market should present an attractive opportunity when reviewed with strategic environment tools.

CSF(R) B3 - The market should be home to a number of cash rich existing or capable franchises with the ability to develop the skills required to operate the franchise.

CSF(R) B4 - The market should be able to provide franchisees with a selection of real estate options that aren't prohibitive to profitability.

CSF(R) B5 - The market should not present idiosyncratic challenges preventing the franchisee from importing products.

b. *How do franchisors select the right franchisee?*

The responses in this area were again, very similar. All the interviewees agreed that a carefully planned selection process, utilising a pre-determined franchisee profile (supporting *CSF (H) C1*) provided the best route to selecting franchisees. As a result of these processes none of the interviewees reported any problems with their current partners although one did describe an instance where the wrong choice had lead to difficulties requiring an expensive contract exit.

There was also a good level of agreement about the key features of this profile. Without a doubt the most important thing that the companies looked for was evidence of financial resources, 'deep pockets', however somewhat surprisingly the next most important element was a sense of chemistry with the potential franchisee (supporting *CSF (H) C3*). All the companies required their potential franchisees to submit a business proposal and used this activity to form an opinion on the likely working relationship that would follow any successfully negotiated agreement.

These business proposals were also all designed to allow the candidates to demonstrate their business acumen and understanding of the local market. Three of the interviewees were able to describe instances of how the use of these proposals had made it quite easy to distinguish between candidates who were committed to the brand as a viable business proposition rather than as trophy to add to their kudos in a particular market. In this way the request for business proposals provided evidence to support some of the elements of *CSF (H) C2*.

All the interviewees agreed on the importance of establishing that potential franchisees were competent brand and business managers. This activity tended to happen towards the end of the selection (following a post business proposal prioritisation) through a visit to the locations where the franchisees were already doing business to see, first hand, the quality of their execution in the market. This visit was also able to validate candidate claims relating to access to real estate which provided evidence in support of *CSF (H) B3*.

Whilst all of the interviewees employed a carefully planned approach to selection, company B stood out from the others through their absolute commitment to getting it right. Their philosophy is based on a lengthy selection process that starts with an internal search using the Internet and other global contacts to develop a list of people who they actively approach. They have learned to avoid relationships with PLC's (unless the CEO or Chairman are majority shareholders) because they have experienced frustrations and losses as a result of u-turns by the management of these organisations in response to short-term actions to meet the demands of shareholders.

There was one area that did not feature in the responses from the interviewees but had been a feature in some of the literature reviewed, i.e. *CSF (H) C4* which suggested that franchisors should consider how they market their franchise system and sell it to their prospective franchisees. Therefore on the basis of the responses the original hypotheses can again be refined;

CSF(R) C1- Select franchisees through a planned process that employs a clear franchisee profile detailing the required skills and attributes.

CSF(R) C2 – A franchisee profile should include; access to a reliable source of financial revenue; access to prime real estate; evidence and experience in brand *management; knowledge of the local market; evidence of commitment to developing the brand in the market; and evidence of successful and calculated risk taking.*

CSF(R) C3 - Relationship 'chemistry' should exist with a successful candidate.

iv. Discussion of the results relating to market and franchisee selection

The aim of this element of the research was to derive criteria to be used in market and franchisee selection (including the business proposal structure). The congruence of interviewee responses has enhanced the credibility of these criteria which are now discussed in turn.

a. Market selection criteria

The refined CSFs can be easily translated into market selection criteria, however they do warrant an element of further consideration relating to how some of these criteria can be quantified or detailed.

CSF(R) B1 highlights the importance of brand awareness, demand and market growth. Traditionally brand awareness is measured through market research and in the case of international markets this can be costly; points of particular importance for a loss-making business like BRI.

Measures for growth and demand on the other hand are more readily available to TBG through existing arrangements with market research agencies.

CSF(R) B2 requires that a strategic review of the market environment confirm its attractiveness. One particularly relevant area of this analysis relating to the Middle East is political instability and hence risk. This is often a subjective measure however a conversation with colleagues in the treasury team suggested that a comparison of bond yields for US dollar bearing bonds or individual country credit ratings would provide a relative quantitative comparison of risk.

Additionally any environmental review of this nature must be founded on a sound understanding of the market structure and this demands local intelligence. Hence in recognising that target franchisees must understand the market, the business proposal structure was designed to collect this information, allowing franchisees to use it to demonstrate their levels of understanding.

CSF(R) B3 relates to the availability of suitable candidates and this can easily be established through a desktop review of the profile of the enquiries received by BRI as well as endorsements received through the earlier practitioner interviews.

CSF(R) B4 highlights the critically important issue of retail location. Again this requires a local input and the business proposal structure requires that franchisees provide a review of the real estate opportunities.

CSF(R) B5 represents a critical element of international export. All markets have differences relating to registration and importation requirements, hence it is vital that a review of these requirements is undertaken and again this is an additional feature of the business proposal structure.

b. Franchisee selection criteria

The interviews illustrated beyond any doubt that the most important element of the decision to franchise is the selection of the franchisee(s), which should proceed via a considered process, reviewing candidates against an ideal set of attributes. Hence the following attributes were developed after the interviews, incorporating further details related to the Boots proposition:

- *Existing competence and capability* – Franchisees must have an existing successful retail business. This should demonstrate; an existing value chain infrastructure; an ability to deliver high standards of execution and roll out at pace; and a strong network of contacts providing access to real estate and 'import facilitation'[19].
- *Financial resources* – Franchisees must have access to sustainable sources of capital to support the development of an area / master franchise agreement.
- *H&B Market awareness* – Franchisees must understand the H&B market and its structure. This should include; market size, demographics, economic indicators,

[19] Exportation to a wide number of international markets requires routes to overcome barriers presented by corrupt officials. 'Facilitation' can involve knowing who to contact and what actions are required to ensure shipments are granted passage into the market.

growth and potential; market competitive structure; and entry barriers (including regulations regarding importation, pharmacy ownership).

- *Comprehension of the Boots business model* – Franchisees must demonstrate a sound understanding of the way a future Boots business will operate and present a viable financial model for its operation.

- *Interpersonal chemistry and passion* – Franchisees must demonstrate a passion for the brand alongside the interdependent development of an appropriate business relationship.

These attributes were used as the basis for the structure of the business proposal (Appendix 2) which potential franchisees, shortlisted through a desktop review against these same criteria, were invited to submit.

3. Quantitative review of the GCC markets

i. Market demographics

Secondary information sourced through the U.S. Census Bureau provided the most recent estimate of the total population of the 6 GCC markets. This data (summarised in Table 4) puts the GCC population at c.35 million in 2004, just over half the size of the UK albeit comprised of a much larger proportion of non-nationals.

Country	Estimated 2004 population (Millions)	Percentage nationals	Percentage females	Percentage below 35 years of age	Population growth rate 1990-2000
KSA	25.796	66.6 %	45.2 %	78.5 %	3.7 %
UAE	2.524	34.3 %	40.9 %	57.6 %	1.9 %
Kuwait	2.258	36.1 %	39.6 %	71.8 %	- 0.8 %[20]
Oman	2.903	57.1 %	44.3 %	66.8 %	3.6 %
Qatar	0.841	49.1 %	34.7 %	47.7 %	4.4 %
Bahrain	0.677	65.4 %	44.1 %	51.1 %	2.4 %
Total GCC	**34.999**	**57.4 %**	**44.2 %**	**75. 1 %**	**3.27 %**
UK	60.271	91.7 %*	50.5 %	43. 8 %	0.3 %

* Data sourced through www.statistics.gov.uk

Table 4. GCC / UK population figures

Country	GDP / Capita 2003 (conversion rate £1 = $1.85)	GDP growth rate	2003 market size (£Millions at retail prices)		
			Cosmetics, Fragrance and Toiletries	Healthcare	Total
KSA	£6,378	4.7%	£487m	£748m	£1,235m
UAE	£12,540	5.2%	£193m	£191m	£384m
Kuwait	£9,784	4.4%	£101m	£90m	£191m
Oman	£7,243	3.3%	£44m	£32m	£76m
Qatar	£11,621	8.5%	£22m	£45m	£67m
Bahrain	£9,243	3.6%	£26m	£17m	£43m
Total GCC	**£8,070**	**4.8%**	**£873m**	**£1,122m**	**£1.995m**
UK	£14,973	2.1%	£5,373m	N/A[21]	N/A

Table 5. Summary of economic indicators and market sizes

[20] The decline in this decade was a direct result of the 1990 Gulf war after which Kuwaitis remained fearful of further occupation whilst Saddam Hussein remained the ruler of Iraq.
[21] It is not possible to compare UK and GCC Healthcare figures due to differences in the definitions comprising the available data sets.

ii. Market structure and economic indicators

The absence of the cosmetics and fragrance categories from the AC Nielson data drove the requirement to combine data from a number of sources to develop a complete overview of the market structure and key GDP indicators. Table 5 provides a summary of this data[22].

iii. Analysis of the Cosmetics, Fragrance and Toiletries market

Product category	2003 Sales (£Million)	2003 Sales (as percentage of total)
Haircare	£171m	20%
Fragrance	£150m	17%
Colour cosmetics	£123m	14%
Skincare	£102m	12%
Bath/Shower	£85m	10%
Oral hygiene	£85m	10%
Make up	£79m	9%
Mens	£76m	9%
Suncare	£2m	0.2%

Table 6. Cosmetics, Fragrance and Toiletries category participation (GCC markets 2003)

The high-level market data was further interrogated to understand the relative sizes of the product categories in the cosmetics, fragrance and toiletries market. The results of this deeper analysis are summarised for the region in table 6 (Appendix 5 provides a full country-by-country breakdown, by channel).

[22] Data sources, Euromonitor Middle East, AC Nielson, National Pharmaceutical Industries, http://www.worldfactsandfigures.com/gdp_country_desc.php, http://www.keynote.co.uk/, http://www.photius.com/rankings/economy/.

The AC Nielson data also provides a consumer sales segmentation by channel for the toiletries categories[23]. These channels are broken down into three types (Table 7); SM (supermarkets and co-ops, greater than 500m2), MM/G (minimarkets, grocers, co-ops and beauty specialists less than 500m2) and Ph (pharmacies).

Product category	Total GCC sales (£Million, 2003)	Channel percentage of total GCC sales		
		SM	MM/G	Ph
Haircare	£171m	47%	35%	18%
Skincare	£102m	48%	33%	19%
Bath/Shower	£85m	57%	40%	3%
Oral Hygiene	£85m	55%	38%	8%
Mens	£76m	59%	36%	5%
Suncare	£2m	56%	20%	24%
Total Toiletries	£521m	52%	36%	12%

Table 7. GCC Toiletries channel structure

iv. *Analysis of the healthcare market* 24

IMS health suggests that the GCC healthcare market has grown at around 10% for the past 5 years and it expects these levels to be maintained over the next few years. The market is far less developed than the UK market with little health education resulting in a high incidence of lifestyle related conditions such as diabetes and respiratory ailments (e.g. Kuwait has the largest per capita incidence of diabetes in the world). This lack of development is related to the fragmentation of the market caused by government regulations, which present barriers to multiple pharmacy ownership. However there are examples of firms who have overcome these barriers to create chains of pharmacies in each of, but not across the GCC markets (e.g. Al Nahdi in KSA with a chain of over 300,

[23] AC Nielson do not report on the cosmetics and fragrance markets, hence the channel summary could only detail the sales split for the toiletries product categories.

[24] Public information relating the GCC healthcare market is limited and as a result this area of analysis is restricted in many areas, to information gained through correspondence with colleagues who have worked in and visited the region.

Al Ghanim in Kuwait with a chain of around 20 and Bin Sina in UAE with a chain of over 20).

Country	Number of Pharmacies	People per Pharmacy
KSA	3,450	7,477
UAE	500	5,048
Kuwait	170	13,282
Oman	300	9,676
Qatar	95	8,852
Bahrain	65	10,415
Total GCC	**4,480**	**7,812**
UK comparison	12,000	4,000

Table 8. Comparison of numbers of pharmacies across the GCC

It is estimated that there are currently around 4500 pharmacies in the GCC which equates to one per 7,812 people, the lowest ratio (Table 8) can be seen in UAE, however this is still much higher than a more developed market like the UK which enjoys a ratio of one per 4,000 people as a result of its 12,000 pharmacies (Numark).

v. *Quantification of brand awareness*

The earlier discussion has illustrated the importance of quantifying levels of brand awareness as part of understanding new market attractiveness. Ideally this area of the research would have utilised focus groups and other market research techniques however the absence of any budget for this required a readily available proxy for this measurement.

Most recognised UK retailers engage a company to manage applications to reclaim VAT on purchases made from them in the UK, by overseas visitors and BTC is no exception to this. Hence it has been possible to access the data relating to the volumes of reclamation split by nationality and as this is related to purchase volumes by these non UK residents, it gives an indication as to the relative amounts of purchases by different nationalities when visiting the UK. Therefore if one is willing to accept that a volume of purchases is a measure of familiarity with the brand, this data has a value as a proxy for a relative level of brand awareness. Table 9 details this data and shows that the combination of just 3 of the markets represents the highest percentage of any nationality claiming refunds on purchases from BTC.

Country	Total BTC retail sales submitted for refunds	Percentage of total
UAE/Kuwait/KSA	£216,767	16.7%
China	£121,369	9.4%
India	£105,985	8.2%
Nigeria	£101,620	7.8%
Hong Kong	£65,657	5.1%
Others	£685,131	52.8%

Table 9. Global comparison of volumes of VAT refunds on BTC sales (source, Global Refund 2004).

vi. Estimations of market risk

The earlier discussion also highlighted the value in estimating the degree of political risk in the markets. The following data (Table 10) details Moody's credit ratings for each of the GCC countries and TBG in an attempt to provide a comparison of GCC market risk with an appropriate internal measure.

Country	Moody's rating (June 2005)	Capacity to repay dept
KSA	Baa2	Adequate
UAE	A1	Good
Kuwait	A2	Good
Oman	Baa2	Adequate
Qatar	A3	Good
Bahrain	Baa1	Adequate
TBG comparison	Baa1	Adequate

Table 10. GCC countries credit ratings

vii. Review of quantitative analysis against market selection criteria

This review established the validity of inviting potential franchisees to prepare business proposals so that further data could be gathered to inform a GCC operating model. The analysis presented in Table 11 reviews the data gathered above, against the criteria refined earlier and clearly indicates the value in progressing the methodology.

Market selection criteria	Initial evidence supporting the attractiveness of the GCC
CSF (R) B1	VAT reclamation figures indicate GCC nationals account for nearly 20% of all BTC retail export scheme purchases. GCC population growth rates are 10 times that of the UK. GCC GDP growth rates are twice that of the UK. The market appears to be capable of supporting a larger number of pharmacies (1 per 7,800 people currently). The total market size is over £2 billion per year, establishing a business with the same market share as BRT have would generate retail sales in the order of £60 million per annum and estimated revenues for BRI of £3 million (based on a 5% royalty).
CSF (R) B2	The market financial risk appears to be similar to that of TBG.
CSF (R) B3	BRI's database has significantly more enquiries from this region than any other globally. Practitioner interviewees confirmed that the region is home to some of their most capable franchisees.
CSF (R) B4	Practitioner interviews and speculative enquires illustrate the substantial degree of retail location development underway in the region, as it seeks to move away from its dependency on wealth through oil production.
CSF (R) B5	Remains largely undefined, however testimonials from the practitioners indicate the same FMCG products are available in the market as sold by BRT.

Table 11. Review of initial quantitative data against market selection criteria

4. Franchisee candidate business proposals

A desktop review (using the earlier selection criteria) of the BRI database and other potential candidates highlighted by the practitioner interviewees generated a shortlist of 12 potential franchisees, who were invited to prepare business proposals in line with the structure developed in step 3 (Appendix 2).

i. Analysis of the proposals received

5 of the 12 candidates accepted the invitation to prepare business proposals and each of these has been summarised in Appendix 5. The following analysis compares each section of the proposals and highlights their key features.

a. Existing competence and capability

Candidate	Key attributes
1	Operates a large number of GCC fast food franchises supported by established pan-gulf infrastructure. GCC consumer (2 million) database with insights from the fast food businesses, many located in shopping mall locations. Strong network connections and influence in the region.
2	Retail franchise experience in the automotive and sporting goods markets. Owner operators of a small (21) chain of pharmacies in UAE. Pan-gulf pharmaceutical distribution business. Experience in registration and de-regulation of pharmaceutical products in the region. Strong relationship with the ministries of Health across the GCC.
3	Retail franchise experience through a small number of well-known western brands. Operations supported by JV with world-renown logistics provider and cutting edge SAP based enterprise resource system. Excellent relationships with property developers across the GCC (outside of KSA), including owning a number of malls themselves. 'In house', marketing agency and specialised retail HR practices.
4	Significant influence through networks across the region and beyond. Operation of a number of franchise systems through interests in the automotive, fast food and hotel industries. Ownership of a number of chains of pharmacies in UAE (46). Additional business interests in real estate management, oil production.
5	Currently operating over 40 western retail brands through franchise agreements including MAC cosmetics, Debenham's (affording access to a wide range of premium brand cosmetics) and the Body Shop. Comprehensive retail support and logistics infrastructure in place pan-gulf. Excellent connections with property developers (often their largest tenants). Controlling shares in 2 marketing (PR & media) agencies.

Table 12. Comparison of candidate profiles

The review of the first section of the proposals illustrates why the candidates made the shortlist. Of significant note are the facts that two candidates (2 & 4) currently own pharmacy chains and two other candidates (3 & 5) are currently operating a number of western retail franchises. However, Candidate 5's access to premium cosmetics and fragrance brands is the most significant attribute highlighted by this analysis. This inventory could provide a strong compliment to the Boots own brands as with the larger BTC stores in the UK.

b. *Financial performance*

The review of the candidate's claims relating to recent financial performance shows a healthy cadre of successful and growing businesses. If all the claims are to be believed candidates 4, 1 and 5 are backed by businesses which have significant turnovers that are highly likely to support significant levels of investment.

Candidate	Key attributes
1	Annual turnover of over £500 million, accounts submitted showing a ROCE of 167% and 26% growth in the last financial year.
2	Annual turnover claimed to be around £45 million (42% from pharmaceutical distribution and retail pharmacies) supported by a CAGR[25] of 18% over the last 3 years.
3	Retail turnover claimed to be £150 million annually supported by a CAGR of 15% over the last 3 years.
4	Annual turnover claimed to be over £6 billion.
5	Retail division annual turnover claimed to be over £400 million.

Table 13. Comparison of candidate financial performance

c. *GCC market demographics and economic indicators*

The information provided in the proposals was consistent with that gathered from the UK and provided a good point of triangulation with this data, especially as it had a number of different sources. This congruence meant that there were few significant variances in the data (Table 13) although some candidates did add insights related to expatriate composition, income per capita and inflation figures. Candidate 5 also showed a thorough understanding of the market through commentaries on a country-by-country basis of recent economic performance.

[25] CAGR – Compound annual growth rate

Candidate	Key features
1	No differentiation in the analysis provided (slightly older data than the others)
2	Additional insights relating to sources of expatriates and peculiarities of the distribution of wealth in the region
3	Details of income per capita References to the region's attempts and desire to comply with WTO recommendations and its desire to move away from a dependency on Oil wealth
4	Deeper analysis of expatriate composition particularly the important female component of these consumers Lower level of economic detail provided
5	Details of oil production drivers behind the GDP data Details of market by market; income per capita, GDP growth and inflation Individual market commentaries and historical trends

Table 14. Comparison of candidate analysis of demographic and economic indicators

d. H&B Market awareness

Candidate	Key features
1	No awareness of Health as not interested in this area of the business Limited awareness of C&T market; some good consumer insights but categories missing from analysis Poor analysis of the channel structure in the C&T categories presented (e.g. perfumeries listed with 0% share of perfume sales).
2	No analysis of the healthcare market (other than pharmacy numbers by country and total OTC size) despite owning pharmacies and operating a pan-gulf distribution business. No details of importation regulation requirements or pharmacy controls. Demonstrated a sound understanding of the toiletries market (including brands and channels) through analysis of the AC Nielson data; no data for cosmetics or fragrance.
3	Restrictions on pharmacy ownership discussed but no analysis of the healthcare market. Different data sources (Foreign trade statistics) used to analyse the beauty market along with investigation into market space allocation across channels. Useful hair category insights indicating research into this important category. No retail real estate review presented despite being based in largest growing market. No details of importation regulation requirements or tariffs.
4	Provided a qualitative analysis of the healthcare market lacking any quantitative data. Purchased all the AC Nielson data and submitted it without any analysis. Ignored all other elements in this area but also provided the best insights into the consumer including a detailed picture of the role and lifestyle of women in the region.
5	Healthcare market is reviewed by country and provides the split of OTC to pharmaceutical sales although the definition of these areas is not clear. The restrictions over pharmacy ownership are reviewed as well as full country-by-country commentary on the policies relating to healthcare provision. The proposal provides similar data on healthcare channel structure to the others. The best analysis and understanding of the cosmetics, fragrance and toiletries market. Full channel structure analysis on a market-by-market basis for all six GCC markets. Detailed review of retail real estate and impressive existing property portfolio.

Table 15. Comparison of candidate H&B market analysis

This area started to clarify which of the candidates were the most appropriate. Candidate 5's analysis was significantly better than all the others as it considered each market in turn and covered all of the cosmetics, fragrance and toiletries categories. Candidate 2 also demonstrated a thorough understanding of the toiletries market (which one would expect from a pharmacy operator) although somewhat disappointingly were unable or unwilling to provide a detailed breakdown of the healthcare market; information which should have been available to a credible distributor with their claimed extensive distribution coverage.

Candidate 4's approach offered a very insightful consumer review that described the role of women across the different GCC markets. However this candidate failed to cover a number of other areas in the proposal and chose to simply purchase and submit the raw set of AC Nielson data rather than use it to demonstrate market understanding.

This section started to suggest that candidates 1 and 4, whilst obviously wealthy hadn't really attempted to understand the market for the proposition they were seeking to develop.

e. Business model, development plan and location strategy

The difference between candidates 1 & 4, and the others became even more apparent during the review of the development plan and business model (Table 16). These candidates left out significant areas of the brief, including the royalty structure.

This section of the proposals showed which candidates understood how a Boots system would operate and it was clear which candidates understood retail cost structures, through the accompanying profit and loss accounts (P&Ls). Each of the candidates 2, 3 & 5 chose models based on different store formats (ignoring implants), recognising the need to enter the market with more than one proposition.

There was a temptation to rank the proposals on the strength of their royalty payments however closer inspection of the associated pricing assumptions showed that these levels were broadly similar ahead of detailed negotiations[26].

The exclusion of KSA from candidate 3's plans meant that despite having a highly credible proposal its materiality was significantly lower than those provided by candidates 2 and 5. The direct comparison of these later two proposals shows a significantly higher level of investment from candidate 5 along with much more realistic sales intensities in the stores. It is also noteworthy that candidate 5 is advocating starting with a pilot, ahead of committing this investment, indicating a degree of calculated risk taking.

[26] The apparent attractiveness of a 7% royalty on Boots supplied lines in candidate 5's proposal being supported by a pricing assumption of 10% above UK TISP (Tax inclusive selling price, i.e. including VAT), whilst the other candidates assumed a level at or just below UK TISP.

Candidate	Key features
1	Development plan of 213 doors (mainly implants, only 43 actual stores, 250 –500m^2) generating sales of £93 million by year 5. Assumed 50% BRI supplied sales participation in the stores. Failed to understand the differences between Boots and the fast food industry claiming models were the same. Didn't see pharmacy as a key feature of the model other than as a location for implants. Failed to propose a royalty structure for the business. Equity purchase option agreement in principle.
2	Estimated year 5 sales £141 million. 3 store formats across 91 stores, all with pharmacies and formats partially tailored to location; Mega mall, 300+m^2, Mall, 250m^2 and High Street, 175m2. Ambitious intensities for a new market; £200+/m^2/wk in largest stores. BRI supplied toiletries inventory only. Full P&Ls supplied with acceptable A&P investment and reasonable cost structures. Lowest royalty offered (only 2% of retail), with £10 million capital invested over 5 years. Proposal based on establishing a series of JVs between the candidate and other pharmacy owners across the region (one reason for lower royalty). JV structure reflected in description of resources required. No discussion of equity purchases.
3	Omitted the largest GCCmarket, KSA, hence year 5 sales only £37 million. 2 store formats across 29 stores, all with pharmacies; Malls, 700m^2 and neighbourhoods, 250m^2. Conservative intensities of £60/m^2/wk (lower than Thailand). Indicative P&L supplied with acceptable A&P investment and reasonable costs. Royalty of 3% of retail offered with £12 million capital invested over 3 years. BRI resources defined but no indicative brand management structure. Willing to discuss equity purchase further.
4	3 formats, 1 store c. 300m^2 and 2 implants, c. 15m^2 & c. 45m^2. Development plan of up to 458 doors (max 84 stores) in 5 years, with retail sales in the order of £60 million at end of year 5. Full P&Ls supplied for stores and implants showing, intensities unlikely to support the stores element of the business (around £30/m^2/wk). Capital investment of £12 million over 5 years No details of resource requirements, royalty structure or equity purchase options.
5	3 store formats, all with a pharmacy, tailored to location as in the UK; Format A, 600m2 (levering their access to premium beauty brands), Format B, 250m2 and Format C, 150m2. Targeted Boots supplied product participation of 45% across the chain, 30% in Format A, 45% in Format B and 50%+ in Format C. Pilot in Kuwait and UAE (in suggested geographies) then roll out to 160 stores over 5 years with projected sales (based on intensities of £100/m2/wk) of £200 million in yr 5. Franchisee capital investment of £100 million. Full P&L's by market detailing A&P at 3% of retail sales. Royalty, 3% of retail sales for locally sourced and 7% of retail sales for BRI supplies. BRI set-up costs funded from a sign on fee and additional layout design fee for each store. Clear picture of resource requirements on both sides.

Table 16. Comparison of candidate business models and development plans

f. Interpersonal chemistry and passion

Candidate	Key attributes
1	Failed to develop relationship, ignored instructions regarding contact protocols, no passion for the retail brand and its proposition. Interest in Boots perceived to be as a trophy.
2	Highly passionate about the Boots brand and worked hard to develop a strong relationship throughout the creation and delivery of the proposal.
3	Undertook a trip to Thailand to understand the BRT operation. Innovative approach to research provided differentiation.
4	Strong relationship developed (although bordering on sycophancy occasionally) Didn't understand the operating model for the Boots brand, despite visiting the BRT operation and a number of teleconferences with the UK. Interest in Boots perceived to be a trophy
5	Highly passionate about the Boots brand all the way to the level of CEO. Candidate has been in dialogue with BRI for over 10 years and still displays energy and enthusiasm for the business. Undertook a trip to Thailand to understand the BRT operation.

Table 17. Comparison of relationships developed during development of candidate proposals

Despite being a highly subjective and intuitive element of the candidate comparisons this area provided a strong degree of congruence with the quality of the proposals. The review of the relationships developed (Table 17) highlights clear distinctions between two sets of candidates. The first set contains three candidates who developed respectful and business-like relationships, whilst the second comprises the other two candidates (1 and 4) who didn't demonstrate any real passion for developing the Boots brand in the region. This latter set failed to grasp the operational complexities and ended up perceived as wealthy 'trophy hunters' looking to bag one of the few UK high street brands who hadn't already entered the region.

g. Proposal ratification through market visit

The review of the proposals demonstrated the quality and suitability of candidate 5 as a potential master franchisee for any Boots entry into the GCC. However at this point in the research very little of the information provided by any candidates had been validated and no final recommendation could be credible without a market visit to ratify the opportunity. A number of the candidates had suggested that a market visit was a suitable next step in the process and as a result a visit was arranged, independently with both candidates 2 (being a clear second in terms of the proposal quality) and 5 targeting the following objectives;

- To understand and visit the candidate's existing retail operations,
- To visit the proposed locations detailed in the business proposals,
- To understand and experience the market opportunity first hand.

The results and observations of these visits completely ratified the data and claims submitted in both the proposals and illustrated the quality of retail execution delivered by both candidates throughout their businesses. The insights gained through the visits were then brought together with the understanding gained from the other business proposals to develop the following environmental analysis.

5. Environmental analysis of the GCC H&B market

The practitioner interviews reinforced the importance of applying strategic market assessment tools in understanding the attractiveness of any new market. This section describes the GCC H&B market environment through the application of both PEST and five forces analyses.

i. GCC PEST analysis

Political/Legal	Economic
Pharmacy licences granted to native applicants only. New premises must be at least 200m away from existing premises. Licences permit ownership of 1 or 2 sites only (differs by country). Product registration requirements follow global norms for most countries, KSA being more involved and time consuming. Religious belief prevents import of porcine or alcoholic products (unless denatured). Retail promotional activity must be registered with the government in Kuwait. Traditionalist religious beliefs drive legal enforcement such that; - Women are forbidden to drive or work in mixed gender environments (including shops), - Women of all nationalities must appear fully covered, in black clothing, when in public, - Shops and businesses close for prayer times during their hours of trade, - Advertising and packaging materials are censored if they contain uncovered images of the female form, - Media censorship is highly prevalent and there is little freedom of speech.	Market risk levels appear to be commensurate with those assigned to the TBG. GDP growth across the GCC is twice that of the UK. Large wealth disparities have created a target consumer population with significant levels of disposable income. Margins on medicinal products are restricted to 20% through government enforcement. There is no VAT or taxation on income in the GCC. The government enforces import tariffs on all foreign goods (5% of the value for Boots supplied ranges). Global supermarkets e.g. Carrefour and Geant are becoming strong players in the H&B market. Strong growth in the H&B market size will continue to be supported for the next few decades by the steadily rising birth rate. Available retail space is increasing at an alarming rate as the region seeks to grow tourism and break way from a dependency on oil production (e.g. 227% in Dubai between 2004 and 2006).
Socio-cultural	**Technological**
There is low awareness of the importance of preventive healthcare and healthy living; the incidence of diabetes per capita is the highest in the world. Conformance with social norms is very important and these norms have the extended family at the epicentre of almost all activities. The role of the extended family and high birth rate is creating a significant demand for children's toiletries, toys and clothing. Large numbers of the affluent members of the population frequently visit the UK and are familiar with the Boots brand and BTC proposition. Beauty is critically important to the Arabian woman as it seen as the route to a successful and healthy marriage. In traditionalist markets the Arabian men do the shopping however this trend is moving with more women joining their husbands in the malls. Western brands are gaining acceptance and are common purchases amongst the target groups. The consumer group is characterised by a high percentage of young people who are eager and promiscuous experimenters displaying little brand loyalty. Coffee bars are important meeting places and footfall drivers having filled the gap occupied by alcoholic bars in the west.	Technology is becoming more acceptable and accessible as a route to stay in touch, e.g. everybody has a mobile phone in the GCC. Internet usage is increasing with over 10% of the population now regular users. Certain areas of the region are pioneering new technology as they seek to become global icons e.g. new airport to accommodate Airbus A380 in Dubai, supported by retinal and fingerprint scanning immigration processes. Pharmacy technology is behind the UK offering a Boots model a significant opportunity. Some processes remain archaic e.g. product registration; UAE ministry estimates processing a maximum of 5 products per week.

Figure 4. GCC H&B market PEST analysis

One of the first observations on reviewing the PEST analysis (Figure 4) is the extent of change occurring away from the very traditionalist culture. This change, led by the progressive nations like Bahrain and UAE is fuelling retail investment and encouraging Arabian women to become more involved in shopping activities. This shift is underpinned by demographic and economic indices which illustrate how the current growth in the H&B market is likely to continue for a good few years to come and why so many other western brands report this to be one of their most profitable overseas markets.

In addition to clarifying a number of opportunities, which are discussed in the following chapter, this analysis was valuable in crystallising a number of risks. Three of these are worthy of further elaboration. The first is related to obtaining pharmacy licences and finding a workable solution to the challenges created by the restrictions regarding multiple site ownership. The presence of other chains in the market indicates that this can be overcome, however it highlights a significance risk should a master franchisee be selected without experience in this area. The second is concerned with the scale of retail development, which is underway in the region. The market visits illustrated without any doubt the enthusiasm for development in the region, however the extent of this development creates a problem in that it is bound to mean winners and losers in terms of shopping mall locations. Hence any entry into this market will need to be supported by a rigorous site selection process to ensure that the brand launch is not jaded by failure due to poor site selection. The final important risk is that of gauging the extent of the change occurring in each market. It is clear to see that each country is at a slightly different point on its evolution and as a result careful consideration is required of what will be tolerated and accepted without alienating the local population. This is again relevant in the selection of master franchisee as understanding the dynamics across the GCC will be critical to the success of any business in the region.

ii. Five forces analyses

The absence of any format offering the 3 in 1 Boots proposition creates a challenge for a five forces analysis of the Boots 'space'. As result two analyses have been prepared which look at the pharmacy and beauty markets separately.

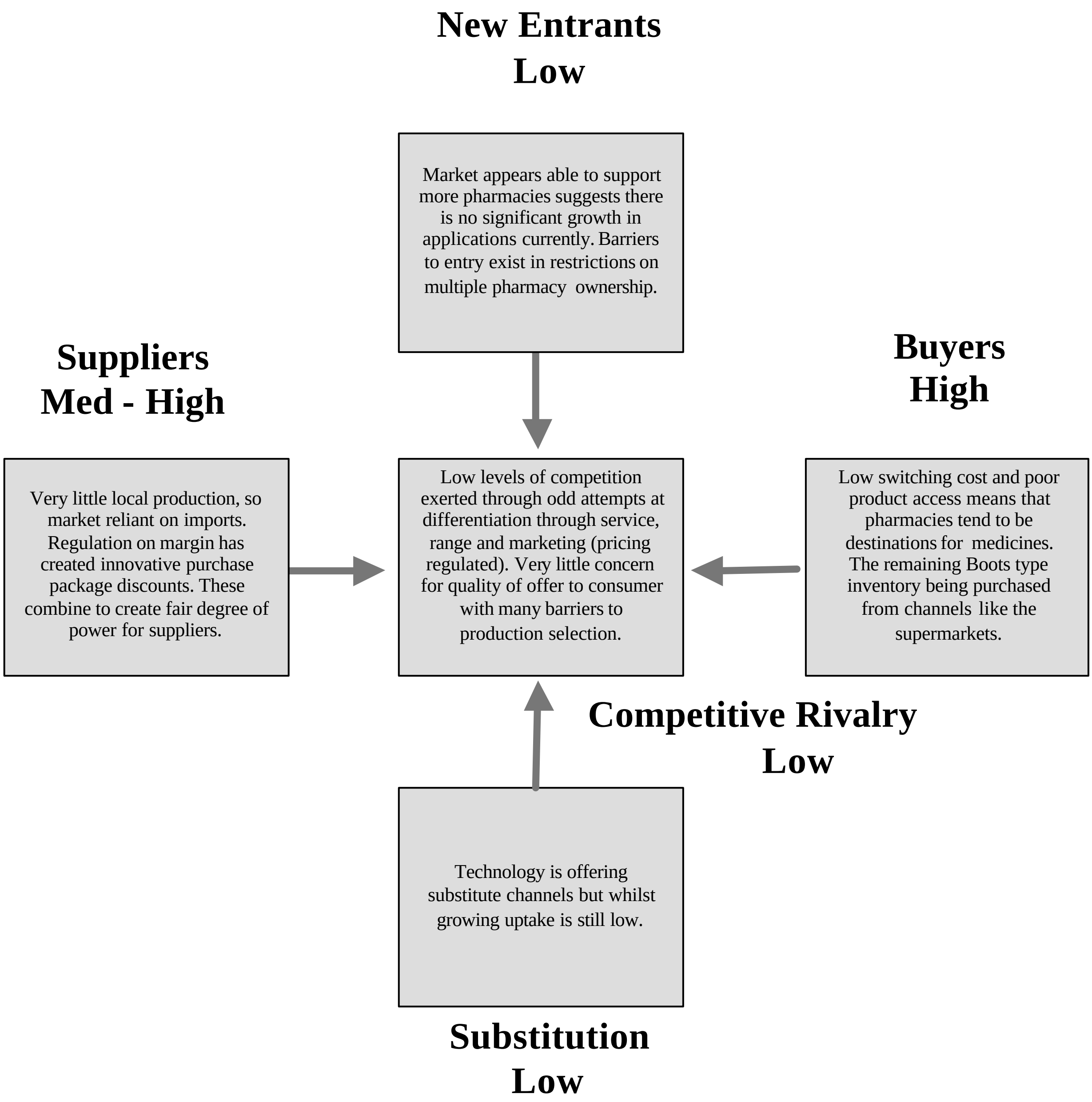

Figure 5. Five forces analysis of GCC pharmacy market

The analysis of the pharmacy market shows how the GCC presents an attractive opportunity for a Boots pharmacy proposition. The power exerted by suppliers could be weakened through a large-scale Boots operation leveraging bulk purchasing. Buyer power is strong because of low switching costs and it is compounded by the high degree of fragmentation in the market (hence low rivalry), which results in little differentiation between pharmacies. This could present an opportunity for a consumer-focused proposition, delivering quality healthcare advice to become a compelling reason for consumers to visit their local pharmacy more often.

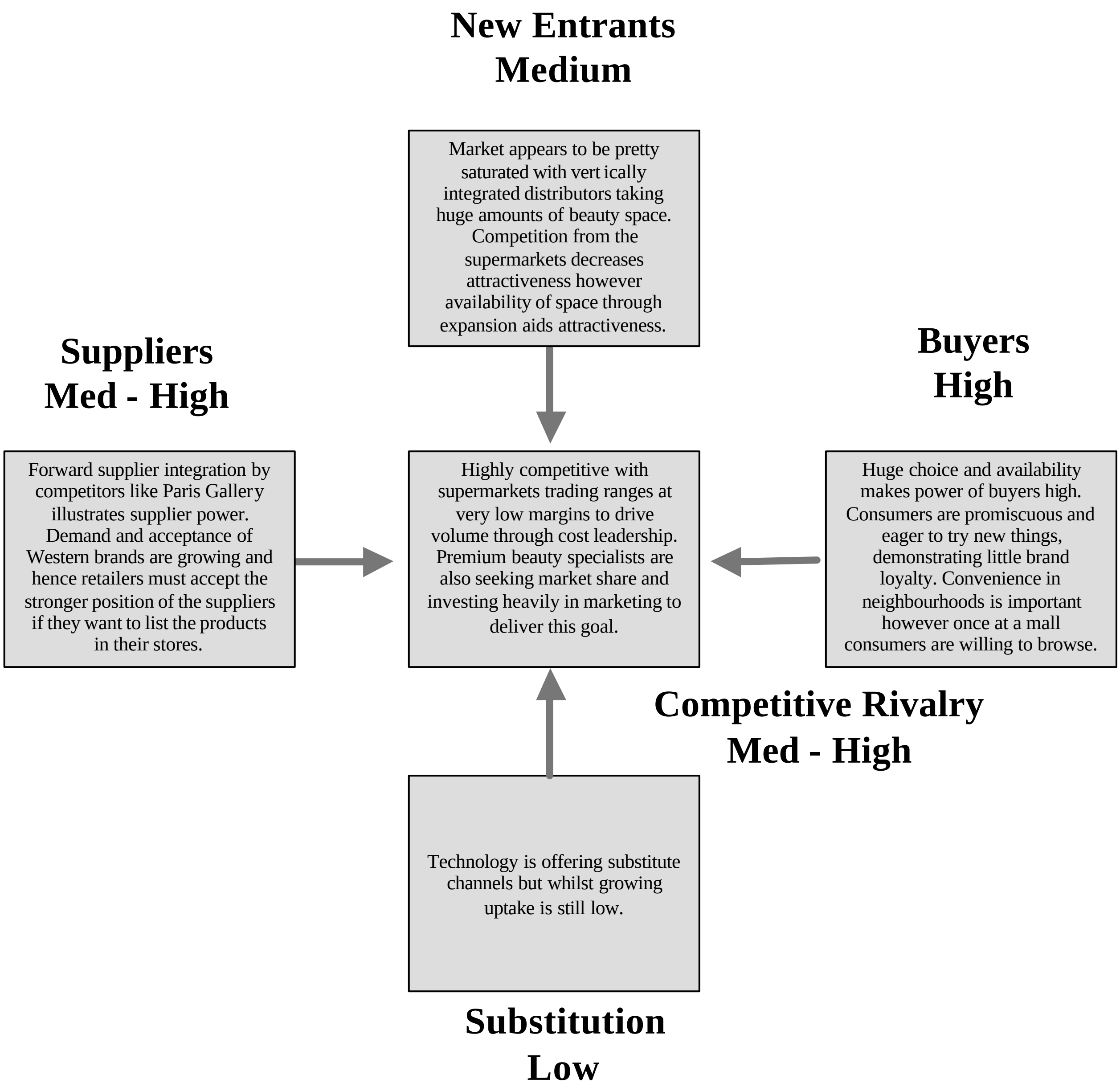

Figure 6. Five forces analysis of GCC beauty market

The analysis of the beauty market indicates a lower degree of attractiveness. Rivalry is fairly intense with the supermarkets leveraging their scale in commodities to drive volumes via cost leadership strategies. Forward integration by suppliers indicates their power and has increased the number of retailers in the market, although observations of their propositions suggest a lack of consumer orientation, highlighting an opportunity to drive business through differentiating on service.

This analysis may however mask an opportunity for Boots in residential and neighbourhood locations. Whilst it is a fair reflection of the scene where most of these items are purchased, i.e. the malls, it is unable to assess the opportunity in the locations around consumer's homes and places of work. The hot climate prevents people from travelling too far and the presence of a large number of neighbourhood 'bakala's' (small pre-evolutionary 7-eleven stores) indicates a high demand for convenience shopping to meet immediate replenishment needs. A Boots system, utilising the experience from operating smaller units in Thailand, could be ideally placed to exploit this opportunity, especially if coupled with a differentiated pharmacy offer.

Therefore this environmental analysis provides support for the suggestion that two or three formats of store are critical in this market, one which establishes the brand presence in the major malls and levers the differentiation provided by the unique Boots products and other(s) which compete for the poorly served convenience market through an offer differentiated by service, consumer lead merchandising and the presence of a respected neighbourhood pharmacy.

6. Financial model for a Boots franchise system in the GCC

Whilst the above analysis has suggested the presence of a number of opportunities that could potentially be exploited by a Boots franchise system, the materiality and profitability of such an enterprise remains undefined. Thus the final section of this chapter draws together all the relevant insights from the above results to develop a model based upon some empirically derived assumptions, to give an indication of the likely value of such a system to both BRI and any potential franchisee. This model is then used to establish the key operating sensitivities used to inform the final recommendations.

i. Sales projections

The key drivers of sales projections are the numbers, sizes and intensities of the store portfolio. The most credible business proposals suggest that there should be two or three formats and the above environmental analysis supports this; indicating that mall formats and neighbourhood formats present the best options for exploiting the opportunity. The GCC market structure indicates the importance of the cosmetics and fragrance market and therefore it has been assumed that the mall format should be similar to the 500m^2 one proposed by candidate 5[27]. BTC's experience suggests that neighbourhood formats can be much smaller than this so it has been assumed that these stores will be between 100m^2 and 250 m^2 depending on the sites available[28].

The contemporary practitioner interviews provided the insight that the GCC market delivers intensities that are comparable to the UK, albeit from slightly smaller formats. Hence for the purposes of the model it has been assumed that each of these stores will deliver intensities of £90/m^2/wk, which is conservative against the UK (c. £120/m^2/wk) but reflecting the fact that one candidate felt the intensities would be lower than the UK.

The store portfolio assumptions have been modelled on the development plan suggested by candidate 5 owing to the fact that this candidate had demonstrated their skill in site selection for their other brands during the market visit. However to retain a conservative projection this plan has been revised down by 25% to include 120 stores over the first five years (Table 18).

Store format	Year 1	Year 2	Year 3	Year 4	Year5	Total
500m^2	3	7	4	6	4	24
250m^2	2	6	12	11	10	41
150m^2	2	8	15	15	15	55

Table 18. Assumptions on store development to year 5

These projected store intensities and opening sequences were then used to build the ten-year series of sales projections in the model assuming sales of six months in the year of opening and an annual inflation rate of 1.5% (weighted from 2004 estimates, source, http:// www. indexmundi.com/)

[27] Healthcare and pharmacy, c40m^2 – based on the BRI Thai store layout; Toiletries and commodities, c200m^2 – based on the BRI Thai layout with more navigation space; and a premium beauty and fragrance area of c250m^2 – based on a similar format to the candidate's in house specialist beauty and fragrance proposition.

[27] For simplicity of modelling these stores have been considered as two formats of c150m2 and c250m2 (the 250m2 being the same as the 500m2 store above but without the premium offer and the smaller being a scaled down version of the 250m2 store retaining Boots brands but decreasing the third party representation).

ii. Operating cost projections

The most significant cost in the model is the cost of stock and in order to estimate these costs it was necessary to make some assumptions on the sales participation of Boots supplied products by format and product margins. The proposal from candidate 2 was used as the basis for the sales participation assumptions along with margin information from Thailand and candidate 5's proposal (Table 19).

Format	Sales participation of Boots supplied products	Costs of Boots supplied products (% of GCC RSP assumed at 10% above UK TISP)	Sales participation of non medical locally sourced products	Average costs of other non Boots products (% of GCC RSP)	Sales participation of medical products	Average costs of medical products (fixed)
500m^2	33%	35%	57%	66%	10%	80%
250m^2	45%	35%	35%	70%	25%	80%
150m^2	50%	35%	20%	70%	30%	80%

Table 19. Margin and sales participation and participation model

Having applied the costs of purchasing products the full cost of sales was completed with an assumption on royalty. The highest royalty suggested in the business proposals was around 5% of sales based on the assumption that retail prices for Boots supplied lines would be 10% above UK TISP (as reflected in the cost prices above). Hence for the purposes of building a model a royalty of 5% of total sales was included to act as a starting point for the later sensitivity analysis.

The remaining costs were taken from the business proposal submitted by candidate 5 (A&P increased to 4% of retail, from the 3% proposed), as they appeared to be reasonably congruent[29] with both experiences in the UK and Thailand. The application of these costs computed a P&L that predicted that the system (before royalty) could

[29] Salary costs appeared to be inflated (UK would be nearer to 8.5%), but it was suspected that this figure was over inflated to allow some movement in the negotiations relating to royalty.

generate an EBIT return on sales into double digits by year 5 with associated revenues for BRI of around £ 6.5 million based on a 5% royalty (Table 20).

Projected GCC franchise system P&L statement (Base case)
CURRENCY: £ 000's

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**4,212**	**21,720**	**53,560**	**91,259**	**129,177**	***100%***	**157,596**	**160,748**	**163,963**	**167,243**	**170,588**
Cost of Goods Sold	2,330	11,959	29,458	50,147	70,957	*55%*	85,811	87,527	89,278	91,064	92,885
Royalty on Sales	211	1,086	2,678	4,563	6,459	*5%*	7,880	8,037	8,198	8,362	8,529
Net margin	**1,671**	**8,675**	**21,424**	**36,549**	**51,761**	***40%***	**63,905**	**65,183**	**66,487**	**67,817**	**69,173**
Staff Costs	472	2,346	5,624	9,400	13,176	*10%*	15,287	15,432	15,740	16,223	16,718
Occupancy Costs	371	1,629	3,589	5,841	8,009	*6%*	9,298	9,484	9,674	9,867	10,235
Controllables	105	543	1,339	2,281	3,229	*3%*	3,940	4,019	4,099	4,181	4,265
Shrinkage	42	217	536	913	1,292	*1%*	1,576	1,607	1,640	1,672	1,706
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**436**	**2,692**	**7,337**	**13,005**	**18,792**	***15%***	**25,591**	**26,820**	**28,246**	**29,713**	**31,073**
Marketing Costs	168	869	2,142	3,650	5,167	*4%*	6,304	6,430	6,559	6,690	6,824
Operations Management Costs	168	586	857	1,004	1,033	*1%*	1,103	1,125	1,148	1,171	1,194
Total Brand Contribution	**99**	**1,237**	**4,338**	**8,351**	**12,592**	***10%***	**18,184**	**19,265**	**20,540**	**21,852**	**23,055**
Retail Brand Management Costs	329	500	589	639	646	*1%*	788	804	820	836	853
Total Retail Profits before Indirect Overheads	**-229**	**737**	**3,749**	**7,712**	**11,946**	***9%***	**17,396**	**18,461**	**19,720**	**21,016**	**22,202**
Logistics Overheads	84	456	750	913	1,292	*1%*	1,576	1,607	1,640	1,840	1,706
Support Function Overheads	72	130	214	274	258	*0%*	315	482	492	334	341
Country Preoperating Expenses	147	174	0								
Total system EBIT profit (before royalty)	**-322**	**1,063**	**5,462**	**11,088**	**16,854**	***13%***	**23,385**	**24,409**	**25,787**	**27,204**	**28,685**
Total Retail Profits before Interest & Tax (EBIT)	**-533**	**-23**	**2,784**	**6,526**	**10,395**	***8%***	**15,505**	**16,372**	**17,588**	**18,842**	**20,155**

Table 20. Indicative P&L for the GCC Boots franchise system

Whilst this conservative financial model indicates that the system has the potential to create significant value, it is predicated upon delivering estimated year 5 sales equivalent to a market share of nearly twice that achieved by the Thai business after 7 years. Therefore a final sensitivity analysis was conducted to determine the key drivers and implications of achieving differing levels of market share as a result of breaking the assumptions underpinning the model.

iii. Results and discussion of the sensitivity analysis

Sensitivity Analysis (Scenarios 1 - 5 and base case)							
	Sales and Profit Drivers	Base Case	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5
	Boots supplied percentage of total retail sales	45%	35%	40%	45%	45%	45%
	Intensity (average £/sqm/wk)	90	90	90	70	80	90
	Number of stores	120	120	120	120	120	100
	Boots Brand Pricing (relative to UK TISP)	+10%	+10%	+10%	+10%	+10%	+10%
	Royalty percentage	5%	5%	5%	5%	5%	5%
Year 5 Key P & L stats	*Total System Retail Sales (£000's)*	£129,177	£129,177	£129,177	£100,471	£114,824	£114,487
	Total landed costs of BRI supplies	£18,602	£14,468	£16,535	£14,468	£16,535	£16,486
	System EBIT Profit (£000's)	£16,854	£12,114	£14,633	£11,495	£14,175	£15,334
	System EBIT as % of Retail Sales	**13.0%**	**9.4%**	**11.3%**	**11.4%**	**12.3%**	**13.4%**
	BRI EBIT Profit (£000's)	£6,459	£6,459	£6,459	£5,024	£5,741	£5,724
	BRI EBIT as % of Retail Sales	**5.0%**	**5.0%**	**5.0%**	**5.0%**	**5.0%**	**5.0%**
	Franchisee Profit (£000's)	£10,395	£5,655	£8,174	£6,471	£8,434	£9,610
	Franchisee EBIT as % of Retail Sales	**8.0%**	**4.4%**	**6.3%**	**6.4%**	**7.3%**	**8.4%**
	Total GCC Market Share	5.4%	5.4%	5.4%	4.2%	4.8%	4.8%

Sensitivity Analysis (Scenarios 6 -11)							
	Sales and Profit Drivers	Scenario 6	Scenario 7	Scenario 8	Scenario 9	Scenario 10	Scenario 11
	Boots supplied percentage of total retail sales	45%	45%	45%	40%	40%	40%
	Intensity (average £/sqm/wk)	90	90	90	80	80	80
	Number of stores	80	120	120	120	120	120
	Boots Brand Pricing (relative to UK TISP)	+10%	par	+5%	+10%	par	par
	Royalty percentage	5%	5%	5%	5%	5%	6%
Year 5 Key P & L stats	*Total System Retail Sales (£000's)*	£92,704	£129,177	£129,177	£114,824	£114,824	£114,824
	Total landed costs of BRI supplies	£13,349	£20,345	£19,532	£14,697	£16,213	£16,213
	System EBIT Profit (£000's)	£11,143	£14,955	£15,989	£12,257	£10,764	£10,764
	System EBIT as % of Retail Sales	**12.0%**	**11.6%**	**12.4%**	**10.7%**	**9.4%**	**9.4%**
	BRI EBIT Profit (£000's)	£4,635	£6,459	£6,459	£5,741	£5,741	£6,889
	BRI EBIT as % of Retail Sales	**5.0%**	**5.0%**	**5.0%**	**5.0%**	**5.0%**	**6.0%**
	Franchisee Profit (£000's)	£6,508	£8,496	£9,530	£6,516	£5,023	£3,875
	Franchisee EBIT as % of Retail Sales	**7.0%**	**6.6%**	**7.4%**	**5.7%**	**4.4%**	**3.4%**
	Total GCC Market Share	3.9%	5.4%	5.4%	4.8%	4.8%	4.8%

Table 21. Sensitivity analysis

The above sensitivity analysis (see Appendix 6 for full P&Ls) extends across 11 scenarios each providing a variation from the base case. The first two scenarios show how reducing the sales participation of the higher margin products supplied by Boots has a significant effect on the overall system profitability, i.e. a 5% decrease generates a drop in the profit to sales percentage of nearly 2%. Whilst this doesn't impact the returns for BRI it does significantly reduce the profits for the franchisee.

The second two scenarios illustrate how failing to reach the targeted sales intensities will reduce the overall sales generated by the system. They show how intensities of £10 and £20 less, per m^2 per week, generate year 5 sales of approximately £15 and £30 million lower than the base case, again resulting in lower profits for the franchisee. The following two scenarios illustrate how a similar result occurs when the numbers of stores (and appropriate portions of costs) are reduced.

The final individual scenarios illustrate the importance of price positioning for the Boots supplied products. The base case assumes that margins can be maximised by pricing the Boots supplied lines at 10% above the UK. These scenarios show (assuming there is no corresponding increase in volumes) how needing to reduce the prices to a level nearer to UK prices could result in year 5 profits around £2 million lower than the base case suggests.

A further important feature of these scenarios can be seen when looking at the distribution of profits between BRI and the franchisee. In the base case the franchisee receives much more than BRI, however as the drivers are reduced the franchisee profits fall rather than BRI's because of the fixed royalty payment. The practitioner interviews suggested that the franchisor should seek to obtain between a third and a half of the system profits and these scenarios show BRI would achieve this through a 5% royalty, although they also suggest, as indicated earlier, that there is more to push for as part of further negotiation if the base case sales assumptions are to be believed.

The final scenarios illustrate the impact of failing to meet the base model intensity as well as needing to reduce the pricing. In the worst case of these, scenario 10, total system year 5 profits are nearly £6 million lower than the base case as a result of following UK pricing in stores with lower intensities. The majority of these reduced profits are incurred by the franchisee and this along with the final scenario highlight the importance of agreeing a royalty rate which will still make the system attractive for the franchisee or being willing to work with them to review the royalty in the event of the system failing to hit the model assumptions.

7. Summary

This chapter has presented the results of the research conducted for this dissertation. It has shown how the methodology has allowed each research step to inform subsequent activities and act as stage gates to prevent both unnecessary internal expense and ensure the value in inviting external parties to prepare proposals. It has ultimately resulted in the completion of a strategic environmental analysis and a model for a Boots franchise system built upon inputs from experienced retailers in the GCC markets.

Chapter 5

Conclusions and recommendations

1. Prelude

This final chapter details the findings and recommendations of this research by answering the original research questions in turn.

Firstly the earlier analysis is used to provide a recommendation on the validity of franchising a Boots retail proposition based on the associated risks and benefits to TBG. This is then followed by a recommendation relating to the second research objective which utilises a SWOT analysis, informed by the environment review and operational model developed in the previous chapter, to support the validity of the GCC as a suitable test market for this Boots franchise system.

The final summary section provides a reflection on the context of this research as well as brief summary of what has happened following the presentation of the recommendations.

2. Recommendations for objective 1

The results of this research have determined the key criteria (*CSFs (R) A1 – A5*) for successful franchise systems and challenged the BTC model against them. This has highlighted evidence from BTC and BRT, which shows that the brand is both proven and profitable, as well as translatable into formats that can be taught to franchisees. It has however also highlighted the absence of some key critical success factors which are related to the management of the risks associated with TBG undertaking a franchise system and Table 22 details these risks along with recommendations for their management informed by this research.

Risk	Recommended action for management and mitigation
Damage to the Boots brand through franchisee mismanagement.	Ensure franchisees with an exemplary track record of brand management are selected. Ensure the franchise manual is explicit in detailing how the franchisee can use the brand. Establish a robust and rigorous monitoring system. Offer existing Boots employees the opportunity to work for the franchisee as part of the set up and ongoing.
BRI resources stretched too thinly ('summit fever')	Ensure the agreement includes a sign-on fee that will cover the costs of the BRI resources required to set up the market.
Selecting the wrong franchisee	Ensure a process is followed which meets the CSFs laid out in this research.
Failure to locate the right property locations	Provide the franchisee with clear criteria for site selection within the franchise manual. Establish a property sign off process as part of agreeing the contract.
Inappropriate price positioning	Include suggestions on price positioning in the franchise manual. Review pricing and sales performance as part of the ongoing monitoring process.
Honesty of the franchisee in declaring royalty payment amounts	Ensure the contract includes permission for independent auditing of the franchise sales data and royalty payments.

Table 22. Risks associated with franchising for TBG

However in addition to exposing these risks, this research has illustrated a number of areas in which TBG stands to create value as a result of developing a franchise system within the BRI business;

- Appropriate new markets can be tested with zero financial risk,
- TBG support costs will be lower as the franchisee covers the 'in market' support costs,
- Once established the system can be rapidly introduced to other appropriate markets with minimal tailoring,
- This approach compliments the implant model providing a stepping stone to full retail participation through fully owned (where permitted) or partially owned stores (via equity purchase options).

There are very few completely risk-free business decisions and the one facing TBG in relation to franchising is no different. However the summary of risk and benefit analysis laid out above highlights that the risks can be managed in the design of the system and the associated contract negotiations.

The risk relating to summit fever is worthy of further short paragraph to highlight how franchising can potentially create a 'win-win' for BRI in offering both a new model of market entry and affording an opportunity to do so without incurring additional P&L costs, or diverting the resource focused on delivering the implant business. The introduction has explained the importance of ensuring that the US expansion continues to be a success and that funding additional resource from within BRI is unlikely. However the business proposals have highlighted potential franchisee's willingness to either contribute to, or fully fund BRI's set up costs through a franchise 'sign-on' fee. Therefore in negotiating a fee upfront BRI will be able to recruit a dedicated, franchisee funded, team to set up the model and create the associated materials (e.g. operating manual) without incurring any P&L exposure or additional risk to the US expansion.

Therefore if the design manages these risks as described, one can focus on the potential benefits which present a compelling case for the first recommendation of this research, i.e. ***BRI, should develop and test a franchise system which manages the above risks, through a dedicated team funded by a negotiated, up-front franchisee sign on fee.***

3. Recommendations for objective 2

The second objective looked specifically at whether the GCC markets provide BRI with an attractive market to test this franchise system. The evidence presented in Table 11 (Chapter 4) has already illustrated the attractiveness of this market and the business proposals have confirmed the absence of evidence indicating that it could pose any significant product registration challenges for the Boots supplied inventory (passing the challenge of *CSF (R) B5* which remained outstanding).

These business proposals have also confirmed that the markets are populated with highly credible master franchisees who have demonstrated the feasibility of operating a Boots franchise system in the region (through their own discounted cash flow analyses[30]). This feasibility is supported through market environment analyses, which whilst illustrating the competitive nature of the beauty market have also highlighted opportunities that could be exploited with a convenience proposition founded on a strong healthcare offer.

[30] DCF analysis was provided by the candidates who offered full P&L accounts, however as these demonstrated positive NPV's and good IRR's they have not been included in detail in this report.

However there are again a number of threats that present further risks in undertaking a trial in this market. The risks are detailed in the following SWOT analysis, which completes the strategic review and presents a summary of the key opportunities and threats relating to a trial in the GCC markets.

Strengths	**Opportunities**
Availability of credible franchisees in the region. Master franchisee option simplifies monitoring requirements. Franchisee sign on fee funds the BRI resource required to support and deliver the implementation. Boots healthcare and pharmacy heritage underpins the proposition. The Boots proposition can be shaped to meet market consumer demand in both neighbourhood and mall locations.	Existing levels of brand awareness. High percentage of population below 35 years. Absence of VAT supports higher margin. Progressive cultural change embracing western brands. Significant disposable incomes in target population. Low import tariff. H&B market experiencing attractive CAGR. Absence of competitors with a 3 in 1 offer. Highly fragmented and underdeveloped pharmacy / healthcare market. Huge growth in available retail space. Poor consumer awareness of disease management. Role of family and high birth rate support a strong demand for children's products. UAE emphasis on generating higher levels of tourism. Women are becoming more involved in retail activities. Franchisees are willing to agree terms allowing TBG to purchase equity in the operation at a later date.
Weaknesses	**Threats**
Lack of regional healthcare / pharmacy knowledge. Absence of franchise manual and other materials. Boots proposition demands franchisees source significant amounts of inventory locally. Length of contract ties BRI into a agreement that could be costly to exit.	Barriers to multiple pharmacy ownership. Censorship may prevent import of certain Boots packaging. Unexpectedly onerous importation procedures. Competition from supermarkets and other forward integration. Misreading pace of cultural change in each country. Fundamentalist activities or traditionalist beliefs have a detrimental impact on the Boots brand. Financial assumptions relating to sales intensities and sales of Boots supplied inventory are significantly inaccurate Failure to position the Boots brands at the right price.

Figure 7. GCC market SWOT analysis

This analysis further illustrates the opportunity for a Boots proposition in this market and supports the formats described in the financial model;

- The large format (located in premium malls) providing consumers with a differentiated beauty, health and baby proposition, to build brand awareness and compete with the cost leadership strategy of the supermarkets, and;
- The smaller formats capitalising on the fragmented neighbourhood convenience H&B opportunity by providing an offer with vastly improved accessibility.

It also illustrates a number of significant factors which make the GCC particularly attractive as a test market; the presence of capable franchisees who can support BRI in developing a system for further roll out in the future; the fact that the market is characterised by high growth; the very attractive combination of low import tariffs and zero VAT; and a level of existing brand awareness.

The threats posed by the market fall into two areas, those that would be fairly generic e.g. competitive threat from supermarkets and uncertainty around modelling assumptions, and those which are more specific relating to the culture and market legislation. The generic threats will form the basis of the objectives of the pilot and underpin the reasons for needing to test the model, however the specific threats warrant a little more consideration.

The issue presented by the legislation relating to pharmacy ownership can be resolved and the evidence of existing chains in each country (two of whom prepared business proposals) illustrate that this has been done. However it highlights the importance of choosing a candidate who understands healthcare well enough to be able to resolve this challenge for a Boots system. The cultural threats can only be managed by working closely with a knowledgeable franchisee that has an extensive understanding of how the pan-gulf environment is changing and the best ways to exploit these changes in a culturally sensitive manner.

The insights drawn from the SWOT analysis therefore support the second recommendation that, ***the GCC markets do offer BRI with an attractive opportunity to test the pilot providing that a suitable master franchisee can be recruited.*** The specific threats created by this market indicate that in addition to the CSFs described above a suitable candidate must be;

- Willing to fund the BRI set up resource through a franchise sign on fee,
- Be competent in, or buy in experts who are competent in, pharmacy operations across the region and,
- Understand the cultural nuances across the region and how to exploit individual opportunities in a culturally sensitive way.

4. Summary

This chapter has described the recommendations from this research. These support and illustrate the benefits to be gained by TBG in establishing a franchise system for application in support of international expansion and confirm that the GCC is a suitable market to pilot this system. An initial working title for this research suggested that this decision is a 'no brainer' as there have been a number of people within the business who have looked at the opportunities presented in the GCC region and held this view for a number of years.

However TBG has not had a great success record in its international ventures and a senior management team who saw the international business losing nearly £1 million a week not more than four years ago, has correctly urged caution. The recent success of the implant proposition has heralded a new era for BRI that has seen renewed investment to support an ambitious US market entry. This market has provided the supporting functions with a real focal point in the drive towards profitability at a time when BRI has needed to remain incredibly lean to continue the reduction in losses.

Hence whether a 'no brainer' or not the opportunity offered by franchising remained undiscovered. The opportunity to utilise the focus of this research has allowed the business to understand and appreciate the gains to be made by developing this route and as a result recommendations have been presented and signed off by the group board which will mean that a pilot of at least 6 of the first Boots franchised stores will commence trading in Dubai and Kuwait from the end of June 2006.

This pilot agreement follows a successful negotiation with a master franchisee whose selection has been consistent with the CSFs and also meets the additional GCC market requirements described above. It acts as a stage gate to the commencement of a regional development plan across the six countries which will extend to a minimum of 120 stores over 5 years and it will be deemed to be successful if the stores exceed targeted levels of sales intensities and participation of Boots supplied lines. In addition to these target criteria the trial will include regular reviews of price positioning through both data analysis and the use of consumer focus groups.

A key feature that has underpinned this decision is the fact the negotiated franchisee sign on fee will fully fund the BRI resource involved in delivering this exciting new market for the period prior to BRI receiving any revenue and well into the first year of trading. This will ensure that the venture is at worst, P&L neutral. Had this not been the case it is highly likely that the risk of a mishap in the death zone would have seen this opportunity aborted before it started traversing the difficult route to executive committee and group board approval.

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Appendix 1 – Semi structured interview questions

Part 1

What are/were the reasons behind your Company's decision to branch out into an international franchising?

Supplementary – what do you believe are the main benefits of franchising?

What are the risks of adopting this approach to business?

How do you manage/mitigate against those risks?

What would you see as the critical factors for a successful business?

Supplementary - offer any from the list of CSF hypotheses that aren't mentioned

Are there any other elements that characterise successful international franchise systems?

Supplementary – does it have to be based on a proven, profitable and non-imitable proposition?
– does it need to be systemisable and easily translated into formats that can be taught to franchisees?

Do you offer multiple contracts in a region? Why?

Part 2

How do you go about selecting a franchisee? What are the most important things you look for?

Supplementary – offer any areas not volunteered by interviewee for comment

How do you set about identifying markets? What makes for a successful market for your franchise system?

Supplementary – offer any areas not volunteered by interviewee for comment

What other advice would you offer a non-competing company thinking about embarking on international expansion through franchising?

Appendix 2 – Business proposal structure

The following list is intended as an indication of the details BRI will consider in an initial assessment of the feasibility of establishing a franchise business with any partner in the GCC. It is followed by a list of further assumptions, which should be used in any financial modelling submitted in support of this proposal.

Section 1- *Franchisee details*

- Company profile, indicating related competencies and attributes
- Sales turnover and financial background with associated references

Section 2- *Market analysis*

- Market demographics and economic indicators
- Health and Beauty (H&B) specifics
  - Breakdown of the market sector by category
    - Including Healthcare, Cosmetics, Fragrance and Toiletries
    - Key brands in each category
  - Review of channel structure and retail market shares of the above
  - Consumer demand trends
  - Pharmacy ownership regulations and restrictions
  - Import regulations, sales taxation and tariffs
- Property and real estate
  - Principle mall locations and developers
  - Details of existing occupation

Section 3- *Franchise development plan (up to 5 years)*

- Recommendations for formats of the Boots system
  - Store sizes and operating configurations
  - Location strategy
  - Inventory mix
- Development and roll-out plan
  - Sales forecasts
  - Formats and markets

- Locations

- Financial plans
  - Proposed cost structure including royalty fees
  - BRI equity buy in options from Year 6 onwards
  - Advertising & Promotion (A&P) contribution
  - Enterprise profitability estimates
- Resource requirements
  - Franchisee brand management structure
  - Requirements from BRI

Assumptions

1. BRI will supply Boots branded and exclusive products on either an FOB or ex works basis.

   -*Assume all brands and SKUs are available (i.e. zero registration / 3rd party license holder rejections). Franchisees will source proprietary brands locally*

2. BRI prices will be at full cost to BRI, relative to supply route.

   -*Assume cost prices of 35% of UK TESP for each SKU.*

3. Stores in Thailand average 180m^2 (with modest sales intensities - £70/m2/wk, compared to c. £120/m2/wk in the UK) and contain c. 2000 Boots supplied SKUs out of a total of c. 5000.

   -*Assume a Boots supplied sales participation of 40%.*

Appendix 3 – Interviewee responses to the primary drivers for franchising

Posited driver of choice	Company A
Resource scarcity	Only in terms of access to cheaper capital
Agency theory	Not considered a real driver of choice
Risk spreading	Definitely – let the franchisee take the risk
Customer mobility	Yes the brand is known the world over
Others	Not mentioned

Posited driver of choice	Company B
Resource scarcity	Yes – Both in terms of access to capital and access to real estate which is critical to the strategy
Agency theory	Not recognised as a benefit
Risk spreading	Yes – Growth strategy is based around owned stores in low risk, JV's or equity shares in medium risk and franchising in high risk regions/locations
Customer mobility	Recognised as a benefit but risk is the real driver of choice
Others	As a route for rapid expansion, the global presence of this brand is founded upon expansion through franchising

Posited driver of choice	Company C
Resource scarcity	Yes – but mainly capital resource and areas where franchisees can help overcome entry barriers
Agency theory	Not recognised as a benefit
Risk spreading	Yes, this is primary driver for this company
Customer mobility	Not seen as a benefit
Others	No other mentioned

Posited driver of choice	Company D
Resource scarcity	Yes – but mainly capital resource and areas where franchisees can help overcome entry barriers
Agency theory	Not recognised as a benefit
Risk spreading	Absolutely a key driver in the decision
Customer mobility	Not recognised as a benefit
Others	None

Posited driver of choice	Company E
Resource scarcity	Yes – but mainly capital resource and areas where franchisees can help overcome entry barriers
Agency theory	Not recognised as a benefit
Risk spreading	Absolutely a key driver in the decision
Customer mobility	Recognised as a benefit but risk is the real driver of choice
Others	None

Appendix 4 – GCC cosmetics, fragrance and toiletries market structure

£(Millions)	TOTAL UAE	SM	MM/G	PH
Fragrance	**35**	N/A	N/A	N/A
Color Cosmetics	**16**	N/A	N/A	N/A
Makeup	**26**	N/A	N/A	N/A
Total Cos/Frag	**77**	N/A	N/A	N/A
Skincare:	**20**	13	5	2
Haircare:	**35**	21	12	2
Bath/Shower:	**18**	10	9	0
Oral Hygiene:	**22**	12	7	2
Mens Care:	**20**	13	6	0
Sun Care:	**1**	1	0	0
Total Toiletries	**116**	69	40	7
T.C&T	***193***	***N/A***	***N/A***	***N/A***

£(Millions)	TOTAL KUWAIT	SM	MM/G	PH
Fragrance	**13**	N/A	N/A	N/A
Color Cosmetics	**6**	N/A	N/A	N/A
Makeup	**8**	N/A	N/A	N/A
Total Cos/Frag	**27**	N/A	N/A	N/A
Skincare:	**14**	10	3	1
Haircare:	**21**	16	4	1
Bath/Shower:	**14**	11	3	0
Oral Hygiene:	**10**	8	2	0
Mens Care:	**15**	12	3	0
Sun Care:	**0**	0	0	0
Total Toiletries	**74**	57	15	2
T.C&T	**101**	N/A	N/A	N/A

£(Millions)	TOTAL BAHRAIN	SM	MM/G	PH
Fragrance	**4**	N/A	N/A	N/A
Color Cosmetics	**2**	N/A	N/A	N/A
Makeup	**4**	N/A	N/A	N/A
Total Cos/Frag	**10**	N/A	N/A	N/A
Skincare:	**4**	2	1	0
Haircare:	**3**	2	1	0
Bath/Shower:	**3**	2	2	0
Oral Hygiene:	**4**	2	2	0
Mens Care*:	**2**	1	1	0
Sun Care:	**0**	0	0	0
Total Toiletries	**16**	9	7	1
T.C&T	**26**	N/A	N/A	N/A

£(Millions)	TOTAL QATAR	SM	MM/G	PH
Fragrance	**5**	N/A	N/A	N/A
Color Cosmetics	**3**	N/A	N/A	N/A
Makeup	**3**	N/A	N/A	N/A
Total Cos/Frag	**11**	N/A	N/A	N/A
Skincare:	**2**	1	1	1
Haircare:	**2**	1	1	0
Bath/Shower:	**3**	2	1	0
Oral Hygiene:	**3**	2	1	0
Mens Care*:	**0**	0	0	0
Sun Care:	**0**	0	0	0
Total Toiletries	**10**	6	4	1
T.C&T	**21**	N/A	N/A	N/A

*** Mens Care omitted due to limited periodicity**

£(Millions)	TOTAL OMAN	SM	MM/G	PH
Fragrance	**4**	N/A	N/A	N/A
Color Cosmetics	**3**	N/A	N/A	N/A
Makeup	**3**	N/A	N/A	N/A
Total Cos/Frag	**9**	N/A	N/A	N/A
Skincare:	**7**	3	4	1
Haircare:	**9**	3	6	0
Bath/Shower:	**7**	2	4	0
Oral Hygiene:	**6**	2	4	0
Mens Care*:	**6**	2	3	0
Sun Care:	**0**	0	0	0
Total Toiletries	**35**	12	22	1
T.C&T	**44**	N/A	N/A	N/A

£(Millions)	TOTAL KSA	SM	MM/G	PH
Fragrance	**90**	N/A	N/A	N/A
Color Cosmetics	**50**	N/A	N/A	N/A
Makeup	**79**	N/A	N/A	N/A
Total Cos/Frag	**218**	N/A	N/A	N/A
Skincare:	**56**	21	20	15
Haircare*:	**100**	37	36	27
Bath/Shower:	**39**	25	14	0
Oral Hygiene:	**41**	20	17	4
Mens Care:	**32**	16	13	3
Sun Care:	**1**	0	0	0
Total Toiletries	**269**	119	100	49
T.C&T	**487**	N/A	N/A	N/A

*** Hairstyling is excluded from Haircare due to limited periodicity**

SM = Supermarket (>500m2) MM/G = MiniMarket / Grocery (<500m2) PH = Pharmacy

Appendix 5a – Summary of proposal from Candidate 1

Existing competence and capability

This proposal claimed that the candidate is the largest retail and manufacturing conglomerate in the Middle East and North Africa with a retail division based around a portfolio of franchised restaurants extending to over 600 units, in 55 cities, across 13 countries (GCC, Syria, Lebanon, Egypt, Jordan, Morocco, Libya and Iran). The entire operation is said to employ over 25,000 personnel and be supported by an established supply chain infrastructure.

This candidate claimed to have developed a database containing information relating to over 2 million ABC and teenage consumers, regularly used to identify shopping trends and consumer insights, further applied in location and trading decisions. The candidate also claimed to have extensive political connections and networks, affording them access to prime real estate and these claims appear to be validated by the quality of the locations in their existing property portfolio.

Financial resources

The candidate's group accounts detailed a latest annual turnover in excess of £0.5 billion with a 167% return on capital, supported by annual growth of 26%. Majority ownership of the group sits with one of the largest diversified investment conglomerates in the region, headed by an individual quoted as the most influential Arab in the world (Massoud et al, 2005) and included in the top 50 of Forbes' list of individuals with the highest net worth.

GCC market demographics and economic indicators

This proposal provided a high quality analysis of the GCC market demographics that is consistent with the data collected from the UK (albeit that the candidate offered data from 2001). It highlighted the significant levels of expatriates in the region and the high proportion of the population below the age of 35.

This candidate failed to provide any economic indicators as part of their proposal.

H&B market awareness

A limited market structure analysis was provided estimating the GCC market for cosmetics and toiletries at £432 million, split across 5 categories; skincare (18%), shampoo (26%), other haircare (7%), cosmetics 21% and fragrance 28%. This analysis also included a channel structure, which is summarised below in table 23.

Category	Large supermarkets and co-ops	Small self service stores	Pharmacies	Perfumeries	Beauty shops
Skincare	66%	13%	13%	7%	0%
Shampoo	73%	14%	10%	3%	0%
Other Haircare	68%	16%	11%	4%	0%
Cosmetics	40%	0%	0%	0%	60%
Perfumeries	40%	0%	0%	0%	60%

Table 23. Candidate derived channel structure

The proposal highlighted a number of key points within the limited categories considered that provide some useful consumer insights;

- There is a high level of involvement in personal grooming and beauty. This is especially related to short term results, i.e. 'how I can change my looks today', rather than ' how I can look and feel better in 6 months',
- Natural and organic products are receiving an increasingly high demand as anxiousness grows in relation to chemicals,
- There is a huge demand for hair products based on the warm conditions in the region and the fact that many locals wear garments on the head[31].

[31] The hijab in the case of women and the combination of the ghutra, igal and tagiyah for men.

- There is a high and growing demand for skin whitening products (similar to the Far East).

This candidate didn't provide any analysis of the healthcare market and claimed that they weren't interested in operating pharmacies, suggesting that implants be employed within existing pharmacies instead.

Business model and development plan

This proposal suggested that the Boots system should seek to follow a differentiated strategy supported by the high quality service and unique Boots brands within the Boots proposition. This would be best achieved through non-pharmacy drug stores or implants in existing pharmacies, which focused on the categories of skin, hair and cosmetics. The associated development plan extended over five years resulting in 213 doors (of which up to 43 would be stores of between 250 & 500m^2 with the remainder as implants), delivering estimated sales of £92 million in year 5 (representing a market share of 15% at the candidates assumed 10% compound annual growth rate, CAGR). The plan was accompanied with a list of the most important locations and a claim that the candidate had already secured premises in these locations due their existing presence and connections.

The proposal didn't provide any further store details such as estimated intensities, P&Ls or estimates of total capital investment. However it did provide a number of estimates of investments that would be made to support the establishment of the Boots brand in the first year including direct marketing and sampling of c. £350,000 and a year 2 media campaign and loyalty programme costing around £500,000. At this stage the candidate declined to offer a percentage figure for royalty payments but verbally suggested that this 'would not be an issue'.

The candidate indicated that their requirements from BRI would include a veteran Boots Brand franchise manager with experience of opening a Boots franchise aboard plus a UK based team to support the candidate's team in market. Their proposal also reflected an agreement to support future equity purchase by Boots through a process involving an assessment conducted in accordance with industry norms utilising a fair value calculated as a multiple of sales, agreed upon by both parties.

Appendix 5b – Summary of proposal from Candidate 2

Existing competence and capability

Candidate 2 is based in Dubai and their business is comprised of autonomous business units that include retail pharmacies (21 in UAE) and pharmaceutical distribution across the GCC and the Levant (Lebanon, Jordan, Israel and Syria). This distribution network extends to over 95% of all pharmacies in the GCC with an inventory of over 350 internationally recognised SKUs.

The proposal highlighted key strengths and capabilities which included, drug de-regulation, close links with health ministries across the GCC and an online distribution system supporting daily deliveries underpinned by an efficient supply infrastructure. Their retail pharmacy business in claimed to hold an 8% share of the UAE market from an inventory of 6500 SKUs, being advantaged through both location to doctor surgeries and the synergy with the distribution network.

Financial resources

The candidate claimed retail turnover to be in excess of £45 million annually (42% from pharmaceutical distribution and retail pharmacies) supported by a CAGR of 18% over the last 3 years.

GCC market demographics and economic indicators

This proposal provided a high quality analysis of the GCC market demographics that was consistent with the data collected from the UK (being supplied by AC Nielsen). It highlighted the significant opportunities afforded through the youthfulness of the population and the large amounts of expatriates in the region (although it went beyond other proposals in providing the insight that the greatest proportion of these expatriates are from Asia rather than the west).

The economic analysis, including GDP data is consistent with the data gathered in the UK and highlighted the significance of rural agglomerations and large disparities across socio-economic groups.

H&B market awareness

The proposal sized the toiletries (i.e. it excluded cosmetics and fragrance) and OTC market at just over £700m (split 77: 23, C&T: OTC). It concentrated on the key three markets of KSA, UAE and Kuwait, as these comprise 85% of the GCC total. In general it provided a market structure congruent with that derived from the UK gathered data, showing the C&T categories ranked in the order of haircare, skincare, bathing, dental, mens and suncare. These rankings were accompanied with an FMCG brand breakdown and annual growth rates indicating that skincare and suncare have the highest levels of year on year growth, in a total market that is growing at nearly 10%.

The headlines from the highly detailed toiletries channel structure analysis were similar to those developed from the UK data, although they indicated that the market share for pharmacies was higher (at 17%) with supermarkets lower (at 48%). The growth rate data supporting this analysis showed that pharmacies are experiencing the highest growth in market share and that this is supported by the highest rates in each of the toiletries categories covered in this proposal.

Unfortunately despite an obvious healthcare expertise this proposal provided no significant analysis of the healthcare market and it can only be concluded that the candidate was either unable or unwilling to offer this information until a further point in the negotiations (sharing such information could have put them at a disadvantage should Boots enter the market as a competitor).

Business model and development plan

This proposal suggested that the Boots system should build upon the existing brand awareness with a proposition that brings as much Boots branded product as possible to the region. The development plan would deliver this through flagship stores in key malls, with additional stores in secondary malls and high street locations. The numbers of these formats were defined by market and their locations described as;

- Mega Malls, stores of c.300+ m2 located in premium shopping malls,
- Malls, stores of c250m^2 located in secondary shopping malls,

- High Streets, stores of c175m^2 located in neighbourhoods, residential areas or on high streets.

The financial section provided full P&Ls by format for Kuwait, KSA and UAE, detailing 91 stores in maturity (year 5) requiring a capital investment in the order of £10 million. Total retail sales (year 5) were estimated at £141 million with FOB sales from BRI assumed at £11 million (landed cost being 15% higher than FOB giving the candidate a margin of 60% on Boots supplied products). In addition to this annual A&P contribution was listed at 5% of retail sales for the first two years (decreasing to 3% thereafter) and a royalty to BRI of 2% of retail sales was offered following a clarification that BRI would not make any profit on the supply of goods, i.e. reiterating the assumptions accompanying the proposal structure.

This proposal reflected the candidate's strength as a distributor and assumed that on average C&T sales would comprise approximately 50% of the sales and that of these sales BRI supplied products would account for 40% (i.e. 20% of the total sales in the chain). The assumption ignores any provision of Boots products outside of the C&T categories.

The store sales estimates were developed using an innovative formula claimed to be based on their existing businesses that utilised estimations of conversion rates of average passers-by into actual customers, combined with an assumed average transaction value for each of these customers. These assumptions are equivalent to intensities of £200-325/m2/wk in mega malls (depending on size 500m^2 – 300m^2), and £115/m2/wk in other malls and high street locations.

This candidate proposed a different set up to the others by advocating the creation of JVs with the leading pharmacy chains across other GCC markets (besides UAE where they would be the franchisee), as they wouldn't have sufficient resources to fund a full Boots entry. In this instance they would remain the Boots master franchisee offering sub franchises to each of the JVs they create in each market. This structure required a slightly different brand management approach, which was reflected in the resource requirements although also meant that a position on options for Boots to purchase an equity stake was not considered.

Appendix 5c – Summary of proposal from Candidate 3

Existing competence and capability

Candidate 3 is based in the UAE and comprised of autonomous business units which include, real estate (including shopping mall development and retail portfolio management), automotive, electronics and insurance in addition to the operation of 6 retail franchises in many GCC countries (no current presence in KSA).

This group has an established logistics partnership with a world-renowned operator that underpins their pan-gulf (excluding KSA) operation. These operations are based on an SAP platform providing them with cutting edge, integrated enterprise resource technology. The candidate detailed their passion for people and how they have developed specialised human resource practices to ensure their personnel are carefully chosen and adequately developed.

This candidate also described a further differentiating capability in that they own a marketing, communications and PR company that provides them with a deep understanding of the most effective routes to communicate with consumers in the region.

Financial resources

The candidate claimed their annual retail turnover to currently be around £150 million, supported by a CAGR of 15% over the last 3 years. The proposal also claimed that they have a strong financial backing based on their broad business operations, developed over the last 70 years.

GCC market demographics and economic indicators

This proposal provided a high quality analysis of the GCC market demographic and economic indicators highlighting the opportunities relating to wealth, expatriates and the youthfulness of the population. This analysis also referenced the work underway across the GCC involving both legislative reform and creating a complementary enforcement infrastructure to ensure compliance with WTO along with the associated opportunities that are likely to follow.

H&B market awareness

The proposal considered the healthcare and beauty markets separately. The ‘Pharma’ market is estimated using foreign trade statistics (FTS) at £1.911 billion of which £1.146 billion is comprised of retail transactions. The candidate referenced the government restrictions over pharmacy ownership and the fact that the market is almost entirely dependent on imports, however the proposal offered no channel analysis at all. It indicated potential opportunities for a credible healthcare offer, which would fill the gap currently observed, for a friendly and professional pharmacy providing advice on common ailments, healthy living and preventative medicine.

The beauty market analysis was presented without AC Neilson data and as such is a useful triangulation. This candidate used FTS, which size the beauty market at £1.1 billion and divide it across the GCC in similar proportions to AC Neilson. However the proposal offered an in house analysis of the channel structure that painted a very different landscape to AC Neilson’s and suggested that the specialist beauty stores are enjoying as a high a market share as the supermarkets. This proposal also reviewed the space allocated to the beauty categories by the key players in the market and this data again shows a degree of consistency with AC Nielson (see summary below, Table 24).

Category	% Available market space	AC Nielson sales participation
Fragrance	23%	17%
Haircare	20%	20%
Cosmetics*	14%	14%
Makeup	N/A*	9%
Bath/Shower	11%	10%
Oral Hygiene	11%	10%
Skincare	9%	12%
Men's	9%	9%
Suncare	2%	0%

* Cosmetics space reviewed is not separate to Make-up

Table 24. Category market space analysis

This proposal didn't review the retail real estate landscape despite the comprehensive beauty competitor review and also missed any reference to import regulations. It did however provide some noteworthy consumer trends in the hair category indicating some research that was different to the other candidates;

- The average GCC consumer spends more on hair colourants (47%) than on shampoo and conditioners (35%) and hairspray (17.5%),
- 10-12 brands account for 75% of sales in the category,
- Brylcreem Hair cream is the leading product in the conditioning segment – highlighting the role of men as shoppers.

Business model and development plan

This candidate's business model is based on 2 proposed store formats, one c700m^2 (in premium locations) and the other c250m^2 (located in neighbourhoods and residential areas), with intensities of c. £60/m^2/wk. Recognising their lack of capability in KSA the proposal was limited to the other 5 GCC markets which make its materiality much smaller as in maturity (year 5) the development plan extends to only 29 stores (whose locations are identified geographically) with combined retail sales of £37 million.

The proposal included a full indicative P&L based on sensible inventory and operating assumptions, which illustrate a sound understanding of the store and support costs required to set up and operate a Boots franchise based on their proposed formats. It detailed a proposed investment of over £12 million during the first 3 years, A&P investment equal to 3% of retail sales and total revenue for Boots of £4 million over the first 5 years through a royalty of 3% of retail sales.

The business proposal also detailed the candidates desire for a ten-year agreement with an automatic renewal clause and their willingness to discuss an equity purchase formula as part of further negotiation. It was however lacking in any indication of the brand management structure despite giving a high level view of the support required from BRI.

Appendix 5d – Summary of proposal from Candidate 4

Existing competence and capability

Candidate 4 is based in UAE and this company forms part of the interests of the ruling family in this part of the region. The sensitivity of this situation meant it was not possible to get a full description of the competencies at this preliminary stage of the investigation, however this candidate confirmed that the interests of the organisation included, oil production, property and shopping mall development, retail pharmacy operations (46 in UAE), schools and franchises for both fast food and hotels. This candidate's proposal didn't provide any further data relating to their competencies and capabilities

Financial resources

The candidate reported the total turnover of organisation business to be in the order of just over £6.2 billion per annum, however there were no financial details provided to support this claim.

GCC market demographics and economic indicators

This proposal provides a similar analysis of the GCC demographics highlighting the opportunities relating to expatriates and the high levels of disposal income. However it differs from the first three proposals in looking at the female numbers in more detail, using AC Nielson data to build a picture of the numbers of both Arabian and expatriate women in each market. This analysis shows that there are significantly more expatriate women than Arabian women in three of the markets, UAE (988,000: 232,000), Kuwait (610,000: 429,000) and Qatar (217,000: 92,000).

H&B market awareness

The H&B analysis also took a distinctly different approach to the other candidates' proposals. This candidate purchased the suite of AC Nielson and submitted it raw with the proposal without any overt analysis, choosing instead to concentrate on the peculiarities of the market and its consumers. Whilst this approach deviated from the proposal structure it was helpful to the entire research piece in that it provided a number of market insights, which were absent from the other proposals. However on the other hand this approach meant that the proposal failed to provide any of the analysis relating to H&B categories, channels or real estate defined in the proposal structure, in what could have been interpreted as arrogance on the part of the candidate.

Business model and development plan

Three types of formats form the basis of this model. The first is a store based on a 250-350m2 Boots format with around 6000-7000 SKUs, positioned as a H&B store with a pharmacy, and located in shopping mall and key high street locations. The other two formats would be implants within existing pharmacies or department stores, one of c45m2 and the other c15m2.

The candidate proposes to form strategic alliances with key players across the region so that they could expedite roll out following a successful pilot across the region. The proposal provides two scenarios that estimate the number of doors after 5 years at between 334 (with 59 stores) and 458 (with 84 stores). The revenue for Boots would be through a mark up on the sales of the Boots branded products that are estimated to generate retail sales by year 5 of between £34 million and £60 million, depending on the scenario.

Appendix 5e – Summary of proposal from Candidate 5

Existing competence and capability

Candidate 5 is based in Kuwait and is comprised of five other divisions (including hotels, automotive and real estate) in addition to its retail arm. The retail business unit is currently split across five sub-divisions; Fashion and Footwear, Food Services, Casual Dining, Health and Beauty, and Optics. In total these sub-divisions include 43 retail brand franchises extending to 700 retail stores across 10 markets (Cyprus, Lebanon, Jordan and Turkey, in addition to the entire GCC).

The retail business is supported through a head office offering centralised business development (including M&A), supply, IS, HR, finance and property functions as well as extensive dedicated brand management teams, which in turn have their own field management structures. This candidate has extensive networks and strong relationships with retail property developers underpinned by the fact that in many cases they are their largest tenants. The strength of this influence is illustrated by the fact that their CEO is also listed in the top 50 most powerful Arabs in the world (Massoud et al, 2005). This candidate's capability is also augmented by the ownership of controlling shares in two marketing agencies, which offer their brands creative, PR and media solutions.

Financial resources

The retail division is claimed to have a turnover of over £400 million and current strategic plans are targeting £ 0.5 billion within the next two years.

GCC market demographics and economic indicators

This proposal provides a comprehensive analysis of the demographics and economic indicators for both the entire GCC and each individual country. The analysis of each country provides a commentary on recent economic trends, inflation and GDP growth rates in addition to a summary of the oil and natural gas production levels supporting most of the GDP.

The analysis in this section was also linked to the H&B market analysis providing further insights into which elements of the population are active in which categories.

The data provided was consistent with the data gathered from the UK confirming an accurate demographic picture for this research.

H&B market awareness

The H&B market analysis reviewed both areas separately. IMS data was used to provide an overview of the healthcare market confirming the market size information gathered in the UK. This overview included a detailed review of the pharmacy channel structure by country, which highlighted the barriers to multiple pharmacy ownership and requirements for licences to be held by nationals. Again a detailed breakdown of healthcare category participation was absent suggesting, in the light of the comprehensive analysis provided by this proposal, that such data is not readily available in the market.

This proposal was the only one to provide a comprehensive review of all the cosmetic, fragrance and toiletries categories (drawing on the experience of operating premium cosmetics and toiletries franchises through, Debenham's and The Body Shop). As with the rest of the proposal it was presented on a market-by-market basis, detailing sizes, growth, channel structure, top selling brands and consumer trends. The candidate also provided a detailed description of the registration processes and documentation required to import the products into each market, along with the detail of import tariffs in the region.

Business model and development plan

The business model underpinning this proposal was supported by three core formats (a fourth implant format was offered for comparison but the estimated contribution lead to the candidate rejecting it). These formats all contained pharmacies (either as a result of licences purchased outright by the candidate or as concessions by inviting existing licence holders to take space in the store) and were described as;

- Format A, stores of c.600 m2 located in premium shopping malls across the region and differentiated through the inclusion of a fragrance and premium beauty area,

- Format B, stores of c.250m2 located in secondary malls and neighbourhood areas and,

- Format C, stores of c.150m2 located in residential areas.

The development plan extended to 150 stores over five years, a candidate investment of £100 million, commencing with a pilot in Kuwait and UAE, before going on to the rest of the GCC markets. The proposal provided the details of which locations the candidate would target as sites for the pilot stores.

The proposal was accompanied by full country-by-country P&Ls breaking down the full costs of the operation (to the detail of staffing structures) and estimating total retail sales of £200 million (a 10% market share) at maturity. The P&Ls also included an annual A&P investment equivalent to 4% of total retail sales, which would be augmented with a further £500,000 to provide a brand launch campaign.

This candidate proposed to pay BRI a royalty on total sales that equated to 7% on Boots supplied products and 3% on all other products sourced from the market. In addition to this the proposal detailed payments to BRI for providing layout design services and an initial ‘sign on’ fee, which would cover all of BRI’s set-up costs up to a maximum limit. The proposal also provided a clear picture of the brand management team that the candidate would hire ‘ahead of the curve’ to support the business in its development to 150 stores and beyond, as well as a set of roles required to support the set-up within BRI.

Appendix 6 - Sensitivity analysis P&Ls

Projected GCC franchise system P&L statement (Scenario 1)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**4,212**	**21,720**	**53,560**	**91,259**	**129,177**	***100%***	**157,596**	**160,748**	**163,963**	**167,243**	**170,588**
Cost of Goods Sold	2,468	12,728	31,386	53,478	75,698	*59%*	92,351	94,198	96,082	98,004	99,965
Royalty on Sales	211	1,086	2,678	4,563	6,459	*5%*	7,880	8,037	8,198	8,362	8,529
Net margin	**1,533**	**7,906**	**19,496**	**33,218**	**47,020**	***36%***	**57,365**	**58,512**	**59,683**	**60,876**	**62,094**
Staff Costs	472	2,346	5,624	9,400	13,176	*10%*	15,287	15,432	15,740	16,223	16,718
Occupancy Costs	371	1,629	3,589	5,841	8,009	*6%*	9,298	9,484	9,674	9,867	10,235
Controllables	105	543	1,339	2,281	3,229	*3%*	3,940	4,019	4,099	4,181	4,265
Shrinkage	42	217	536	913	1,292	*1%*	1,576	1,607	1,640	1,672	1,706
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**298**	**1,923**	**5,409**	**9,674**	**14,051**	***11%***	**19,051**	**20,149**	**21,442**	**22,772**	**23,994**
Marketing Costs	168	869	2,142	3,650	5,167	*4%*	6,304	6,430	6,559	6,690	6,824
Operations Management Costs	168	586	857	1,004	1,033	*1%*	1,103	1,125	1,148	1,171	1,194
Total Brand Contribution	**-39**	**468**	**2,410**	**5,020**	**7,851**	***6%***	**11,644**	**12,594**	**13,735**	**14,912**	**15,976**
Retail Brand Management Costs	329	500	589	639	646	*1%*	788	804	820	836	853
Total Retail Profits before Indirect Overheads	**-367**	**-32**	**1,820**	**4,381**	**7,205**	***6%***	**10,856**	**11,790**	**12,915**	**14,075**	**15,123**
Logistics Overheads	84	456	750	913	1,292	*1%*	1,576	1,607	1,640	1,840	1,706
Support Function Overheads	72	130	214	274	258	*0%*	315	482	492	334	341
Country Preoperating Expenses	147	174	0								
Total enterprise EBIT profit (before royalty)	**-460**	**294**	**3,534**	**7,758**	**12,114**	***9%***	**16,845**	**17,738**	**18,982**	**20,263**	**21,605**
Total Retail Profits before Interest & Tax (EBIT)	**-670**	**-792**	**856**	**3,195**	**5,655**	***4%***	**8,965**	**9,701**	**10,784**	**11,901**	**13,076**

Projected GCC franchise system P&L statement (Scenario 2)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**4,212**	**21,720**	**53,560**	**91,259**	**129,177**	***100%***	**157,596**	**160,748**	**163,963**	**167,243**	**170,588**
Cost of Goods Sold	2,395	12,333	30,374	51,716	73,179	*57%*	89,262	91,048	92,869	94,726	96,621
Royalty on Sales	211	1,086	2,678	4,563	6,459	*5%*	7,880	8,037	8,198	8,362	8,529
Net margin	**1,606**	**8,301**	**20,508**	**34,980**	**49,539**	***38%***	**60,454**	**61,663**	**62,896**	**64,154**	**65,438**
Staff Costs	472	2,346	5,624	9,400	13,176	*10%*	15,287	15,432	15,740	16,223	16,718
Occupancy Costs	371	1,629	3,589	5,841	8,009	*6%*	9,298	9,484	9,674	9,867	10,235
Controllables	105	543	1,339	2,281	3,229	*3%*	3,940	4,019	4,099	4,181	4,265
Shrinkage	42	217	536	913	1,292	*1%*	1,576	1,607	1,640	1,672	1,706
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**372**	**2,318**	**6,421**	**11,435**	**16,570**	***13%***	**22,140**	**23,300**	**24,655**	**26,050**	**27,337**
Marketing Costs	168	869	2,142	3,650	5,167	*4%*	6,304	6,430	6,559	6,690	6,824
Operations Management Costs	168	586	857	1,004	1,033	*1%*	1,103	1,125	1,148	1,171	1,194
Total Brand Contribution	**35**	**863**	**3,422**	**6,781**	**10,370**	***8%***	**14,733**	**15,745**	**16,949**	**18,190**	**19,319**
Retail Brand Management Costs	329	500	589	639	646	*1%*	788	804	820	836	853
Total Retail Profits before Indirect Overheads	**-294**	**364**	**2,833**	**6,142**	**9,724**	***8%***	**13,945**	**14,941**	**16,129**	**17,353**	**18,466**
Logistics Overheads	84	456	750	913	1,292	*1%*	1,576	1,607	1,640	1,840	1,706
Support Function Overheads	72	130	214	274	258	*0%*	315	482	492	334	341
Country Preoperating Expenses	147	174	0								
Total enterprise EBIT profit (before royalty)	**-387**	**689**	**4,547**	**9,519**	**14,633**	***11%***	**19,934**	**20,889**	**22,196**	**23,541**	**24,949**
Total Retail Profits before Interest & Tax (EBIT)	**-597**	**-397**	**1,869**	**4,956**	**8,174**	***6%***	**12,054**	**12,851**	**13,998**	**15,179**	**16,419**

Projected GCC franchise system P&L statement (Scenario 3)

CURRENCY: £ 000's

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**3,276**	**16,893**	**41,658**	**70,979**	**100,471**	***100%***	**122,575**	**125,027**	**127,527**	**130,077**	**132,679**
Cost of Goods Sold	1,813	9,301	22,912	39,003	55,189	*55%*	66,742	68,077	69,438	70,827	72,244
Royalty on Sales	164	845	2,083	3,549	5,024	*5%*	6,129	6,251	6,376	6,504	6,634
Net margin	**1,300**	**6,747**	**16,663**	**28,427**	**40,259**	***40%***	**49,704**	**50,698**	**51,712**	**52,746**	**53,801**
Staff Costs	367	1,824	4,374	7,311	10,248	*10%*	11,890	12,003	12,243	12,617	13,003
Occupancy Costs	288	1,267	2,791	4,543	6,229	*6%*	7,232	7,377	7,524	7,675	7,961
Controllables	82	422	1,041	1,774	2,512	*3%*	3,064	3,126	3,188	3,252	3,317
Shrinkage	33	169	417	710	1,005	*1%*	1,226	1,250	1,275	1,301	1,327
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**285**	**1,816**	**5,040**	**8,979**	**13,002**	***13%***	**18,079**	**19,122**	**20,394**	**21,741**	**23,017**
Marketing Costs	131	676	1,666	2,839	4,019	*4%*	4,903	5,001	5,101	5,203	5,307
Operations Management Costs	131	456	667	781	804	*1%*	858	875	893	911	929
Total Brand Contribution	**23**	**685**	**2,707**	**5,359**	**8,179**	***8%***	**12,318**	**13,246**	**14,400**	**15,627**	**16,781**
Retail Brand Management Costs	256	389	458	497	502	*1%*	613	625	638	650	663
Total Retail Profits before Indirect Overheads	**-233**	**296**	**2,249**	**4,863**	**7,677**	***8%***	**11,705**	**12,621**	**13,763**	**14,977**	**16,118**
Logistics Overheads	66	355	583	710	1,005	*1%*	1,226	1,250	1,275	1,431	1,327
Support Function Overheads	56	101	167	213	201	*0%*	245	375	383	260	265
Country Preoperating Expenses	115	135	0								
Total enterprise EBIT profit (before royalty)	**-305**	**549**	**3,582**	**7,489**	**11,495**	***11%***	**16,363**	**17,247**	**18,481**	**19,789**	**21,160**
Total Retail Profits before Interest & Tax (EBIT)	**-469**	**-295**	**1,499**	**3,940**	**6,471**	***6%***	**10,235**	**10,996**	**12,105**	**13,286**	**14,526**

Projected GCC franchise system P&L statement (Scenario 4)

CURRENCY: £ 000's

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**3,744**	**19,307**	**47,609**	**81,119**	**114,824**	***100%***	**140,086**	**142,888**	**145,745**	**148,660**	**151,633**
Cost of Goods Sold	2,072	10,630	26,185	44,575	63,073	*55%*	76,277	77,803	79,358	80,945	82,564
Royalty on Sales	187	965	2,380	4,056	5,741	*5%*	7,004	7,144	7,287	7,433	7,582
Net margin	**1,485**	**7,711**	**19,044**	**32,488**	**46,010**	***40%***	**56,805**	**57,941**	**59,100**	**60,282**	**61,487**
Staff Costs	419	2,085	4,999	8,355	11,712	*10%*	13,588	13,717	13,992	14,420	14,860
Occupancy Costs	329	1,448	3,190	5,192	7,119	*6%*	8,265	8,430	8,599	8,771	9,098
Controllables	94	483	1,190	2,028	2,871	*3%*	3,502	3,572	3,644	3,717	3,791
Shrinkage	37	193	476	811	1,148	*1%*	1,401	1,429	1,457	1,487	1,516
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**360**	**2,254**	**6,189**	**10,992**	**15,897**	***14%***	**21,835**	**22,971**	**24,320**	**25,727**	**27,045**
Marketing Costs	150	772	1,904	3,245	4,593	*4%*	5,603	5,716	5,830	5,946	6,065
Operations Management Costs	150	521	762	892	919	*1%*	981	1,000	1,020	1,041	1,061
Total Brand Contribution	**61**	**961**	**3,522**	**6,855**	**10,385**	***9%***	**15,251**	**16,256**	**17,470**	**18,740**	**19,918**
Retail Brand Management Costs	292	444	524	568	574	*1%*	700	714	729	743	758
Total Retail Profits before Indirect Overheads	**-231**	**517**	**2,999**	**6,287**	**9,811**	***9%***	**14,551**	**15,541**	**16,741**	**17,996**	**19,160**
Logistics Overheads	75	405	667	811	1,148	*1%*	1,401	1,429	1,457	1,635	1,516
Support Function Overheads	64	116	190	243	230	*0%*	280	429	437	297	303
Country Preoperating Expenses	131	154	0								
Total enterprise EBIT profit (before royalty)	**-314**	**806**	**4,522**	**9,289**	**14,175**	***12%***	**19,874**	**20,828**	**22,134**	**23,497**	**24,922**
Total Retail Profits before Interest & Tax (EBIT)	**-501**	**-159**	**2,142**	**5,233**	**8,433**	***7%***	**12,870**	**13,684**	**14,847**	**16,064**	**17,341**

Projected GCC franchise system P&L statement (Scenario 5)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**4,212**	**19,333**	**50,394**	**84,057**	**114,487**	***100%***	**131,244**	**133,869**	**136,547**	**139,277**	**142,063**
Cost of Goods Sold	2,330	10,645	27,717	46,189	62,888	*55%*	71,462	72,892	74,350	75,836	77,353
Royalty on Sales	211	967	2,520	4,203	5,724	*5%*	6,562	6,693	6,827	6,964	7,103
Net margin	**1,671**	**7,722**	**20,158**	**33,665**	**45,875**	***40%***	**53,219**	**54,284**	**55,370**	**56,477**	**57,607**
Staff Costs	404	2,220	5,338	8,470	10,980	*10%*	12,739	12,860	13,117	13,519	13,931
Occupancy Costs	290	1,504	3,258	5,127	6,670	*6%*	7,743	7,898	8,056	8,217	8,524
Controllables	90	562	1,271	2,056	2,691	*2%*	3,283	3,349	3,416	3,484	3,554
Shrinkage	42	193	504	841	1,145	*1%*	1,312	1,339	1,365	1,393	1,421
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**599**	**1,993**	**6,787**	**12,061**	**17,126**	***15%***	**19,928**	**21,017**	**22,327**	**23,703**	**25,000**
Marketing Costs	168	773	2,016	3,362	4,579	*4%*	5,250	5,355	5,462	5,571	5,683
Operations Management Costs	168	522	806	925	916	*1%*	919	937	956	975	994
Total Brand Contribution	**262**	**698**	**3,965**	**7,774**	**11,631**	***10%***	**13,760**	**14,725**	**15,909**	**17,157**	**18,323**
Retail Brand Management Costs	329	445	554	588	572	*1%*	656	669	683	696	710
Total Retail Profits before Indirect Overheads	**-66**	**253**	**3,410**	**7,186**	**11,058**	***10%***	**13,104**	**14,056**	**15,227**	**16,460**	**17,613**
Logistics Overheads	80	462	737	883	1,220	*1%*	1,488	1,518	1,549	1,737	1,611
Support Function Overheads	72	116	202	252	229	*0%*	262	402	410	279	284
Country Preoperating Expenses	147	155	0								
Total enterprise EBIT profit (before royalty)	**-155**	**488**	**4,991**	**10,254**	**15,334**	***13%***	**17,915**	**18,830**	**20,096**	**21,408**	**22,820**
Total Retail Profits before Interest & Tax (EBIT)	**-366**	**-479**	**2,472**	**6,051**	**9,609**	***8%***	**11,353**	**12,136**	**13,269**	**14,444**	**15,717**

Projected GCC franchise system P&L statement (Scenario 6)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**4,212**	**19,333**	**42,847**	**69,157**	**92,704**	***100%***	**103,600**	**105,672**	**107,786**	**109,941**	**112,140**
Cost of Goods Sold	2,330	10,645	23,566	38,002	50,922	*55%*	56,410	57,538	58,689	59,863	61,060
Royalty on Sales	211	967	2,142	3,458	4,635	*5%*	5,180	5,284	5,389	5,497	5,607
Net margin	**1,671**	**7,722**	**17,139**	**27,697**	**37,146**	***40%***	**42,010**	**42,850**	**43,707**	**44,581**	**45,473**
Staff Costs	404	2,011	4,289	6,817	8,784	*9%*	10,191	10,288	10,494	10,815	11,145
Occupancy Costs	290	1,207	2,575	4,070	5,265	*6%*	6,112	6,235	6,359	6,487	6,728
Controllables	90	465	1,021	1,655	2,153	*2%*	2,627	2,679	2,733	2,787	2,843
Shrinkage	42	193	428	692	927	*1%*	1,036	1,057	1,078	1,099	1,121
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**599**	**2,597**	**5,825**	**9,354**	**12,755**	***14%***	**13,831**	**14,771**	**15,956**	**17,232**	**18,458**
Marketing Costs	168	773	1,714	2,766	3,708	*4%*	4,144	4,227	4,311	4,398	4,486
Operations Management Costs	168	522	686	761	742	*1%*	725	740	755	770	785
Total Brand Contribution	**262**	**1,302**	**3,426**	**5,827**	**8,305**	***9%***	**8,961**	**9,804**	**10,890**	**12,064**	**13,187**
Retail Brand Management Costs	329	445	471	484	464	*1%*	518	528	539	550	561
Total Retail Profits before Indirect Overheads	**-66**	**857**	**2,954**	**5,343**	**7,841**	***8%***	**8,443**	**9,276**	**10,351**	**11,515**	**12,626**
Logistics Overheads	80	434	691	829	1,148	*1%*	1,401	1,429	1,457	1,635	1,516
Support Function Overheads	72	116	171	207	185	*0%*	207	317	323	220	224
Country Preoperating Expenses	147	155	0								
Total enterprise EBIT profit (before royalty)	**-155**	**1,118**	**4,235**	**7,764**	**11,143**	***12%***	**12,015**	**12,813**	**13,959**	**15,157**	**16,493**
Total Retail Profits before Interest & Tax (EBIT)	**-366**	**152**	**2,092**	**4,306**	**6,508**	***7%***	**6,835**	**7,530**	**8,570**	**9,660**	**10,886**

Projected GCC franchise system P&L statement (Scenario 7)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**4,212**	**21,720**	**53,560**	**91,259**	**129,177**	**100%**	**157,596**	**160,748**	**163,963**	**167,243**	**170,588**
Cost of Goods Sold	2,388	12,294	30,261	51,470	72,856	*56%*	88,884	90,662	92,475	94,325	96,212
Royalty on Sales	211	1,086	2,678	4,563	6,459	*5%*	7,880	8,037	8,198	8,362	8,529
Net margin	**1,613**	**8,340**	**20,621**	**35,226**	**49,862**	**39%**	**60,832**	**62,049**	**63,290**	**64,556**	**65,847**
Staff Costs	472	2,346	5,624	9,400	13,176	*10%*	15,287	15,432	15,740	16,223	16,718
Occupancy Costs	371	1,629	3,589	5,841	8,009	*6%*	9,298	9,484	9,674	9,867	10,235
Controllables	105	543	1,339	2,281	3,229	*3%*	3,940	4,019	4,099	4,181	4,265
Shrinkage	42	217	536	913	1,292	*1%*	1,576	1,607	1,640	1,672	1,706
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**378**	**2,358**	**6,534**	**11,682**	**16,893**	**13%**	**22,518**	**23,686**	**25,049**	**26,451**	**27,746**
Marketing Costs	168	869	2,142	3,650	5,167	*4%*	6,304	6,430	6,559	6,690	6,824
Operations Management Costs	168	586	857	1,004	1,033	*1%*	1,103	1,125	1,148	1,171	1,194
Total Brand Contribution	**41**	**902**	**3,534**	**7,027**	**10,693**	**8%**	**15,111**	**16,130**	**17,342**	**18,591**	**19,729**
Retail Brand Management Costs	329	500	589	639	646	*1%*	788	804	820	836	853
Total Retail Profits before Indirect Overheads	**-287**	**403**	**2,945**	**6,389**	**10,047**	**8%**	**14,323**	**15,327**	**16,523**	**17,755**	**18,876**
Logistics Overheads	84	456	750	913	1,292	*1%*	1,576	1,607	1,640	1,840	1,706
Support Function Overheads	72	130	214	274	258	*0%*	315	482	492	334	341
Country Preoperating Expenses	147	174	0								
Total enterprise EBIT profit (before royalty)	**-380**	**729**	**4,659**	**9,765**	**14,955**	**12%**	**20,312**	**21,274**	**22,589**	**23,943**	**25,358**
Total Retail Profits before Interest & Tax (EBIT)	**-590**	**-357**	**1,981**	**5,202**	**8,497**	**7%**	**12,432**	**13,237**	**14,391**	**15,581**	**16,829**

Projected GCC franchise system P&L statement (Scenario 8)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**4,212**	**21,720**	**53,560**	**91,259**	**129,177**	**100%**	**157,596**	**160,748**	**163,963**	**167,243**	**170,588**
Cost of Goods Sold	2,359	12,141	29,886	50,831	71,822	*56%*	87,623	89,376	91,163	92,987	94,847
Royalty on Sales	211	1,086	2,678	4,563	6,459	*5%*	7,880	8,037	8,198	8,362	8,529
Net margin	**1,643**	**8,493**	**20,996**	**35,865**	**50,896**	**39%**	**62,093**	**63,335**	**64,601**	**65,894**	**67,212**
Staff Costs	472	2,346	5,624	9,400	13,176	*10%*	15,287	15,432	15,740	16,223	16,718
Occupancy Costs	371	1,629	3,589	5,841	8,009	*6%*	9,298	9,484	9,674	9,867	10,235
Controllables	105	543	1,339	2,281	3,229	*3%*	3,940	4,019	4,099	4,181	4,265
Shrinkage	42	217	536	913	1,292	*1%*	1,576	1,607	1,640	1,672	1,706
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**408**	**2,510**	**6,909**	**12,320**	**17,927**	**14%**	**23,779**	**24,972**	**26,360**	**27,789**	**29,111**
Marketing Costs	168	869	2,142	3,650	5,167	*4%*	6,304	6,430	6,559	6,690	6,824
Operations Management Costs	168	586	857	1,004	1,033	*1%*	1,103	1,125	1,148	1,171	1,194
Total Brand Contribution	**71**	**1,054**	**3,909**	**7,666**	**11,726**	**9%**	**16,372**	**17,416**	**18,654**	**19,929**	**21,094**
Retail Brand Management Costs	329	500	589	639	646	*1%*	788	804	820	836	853
Total Retail Profits before Indirect Overheads	**-258**	**555**	**3,320**	**7,027**	**11,080**	**9%**	**15,584**	**16,613**	**17,834**	**19,093**	**20,241**
Logistics Overheads	84	456	750	913	1,292	*1%*	1,576	1,607	1,640	1,840	1,706
Support Function Overheads	72	130	214	274	258	*0%*	315	482	492	334	341
Country Preoperating Expenses	147	174	0								
Total enterprise EBIT profit (before royalty)	**-350**	**881**	**5,034**	**10,404**	**15,989**	**12%**	**21,573**	**22,560**	**23,901**	**25,281**	**26,723**
Total Retail Profits before Interest & Tax (EBIT)	**-561**	**-205**	**2,356**	**5,841**	**9,530**	**7%**	**13,693**	**14,523**	**15,703**	**16,919**	**18,194**

Projected GCC system enterprise P&L statement (Scenario 9)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**3,744**	**19,307**	**47,609**	**81,119**	**114,824**	***100%***	**140,086**	**142,888**	**145,745**	**148,660**	**151,633**
Cost of Goods Sold	2,130	10,966	26,994	45,994	64,990	*57%*	79,289	80,875	82,492	84,142	85,824
Royalty on Sales	187	965	2,380	4,056	5,741	*5%*	7,004	7,144	7,287	7,433	7,582
Net margin	**1,426**	**7,375**	**18,234**	**31,069**	**44,092**	***38%***	**53,793**	**54,869**	**55,966**	**57,085**	**58,227**
Staff Costs	419	2,085	4,999	8,355	11,712	*10%*	13,588	13,717	13,992	14,420	14,860
Occupancy Costs	329	1,448	3,190	5,192	7,119	*6%*	8,265	8,430	8,599	8,771	9,098
Controllables	94	483	1,190	2,028	2,871	*3%*	3,502	3,572	3,644	3,717	3,791
Shrinkage	37	193	476	811	1,148	*1%*	1,401	1,429	1,457	1,487	1,516
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**302**	**1,918**	**5,379**	**9,573**	**13,979**	***12%***	**18,824**	**19,899**	**21,187**	**22,530**	**23,785**
Marketing Costs	150	772	1,904	3,245	4,593	*4%*	5,603	5,716	5,830	5,946	6,065
Operations Management Costs	150	521	762	892	919	*1%*	981	1,000	1,020	1,041	1,061
Total Brand Contribution	**2**	**625**	**2,713**	**5,435**	**8,468**	***7%***	**12,240**	**13,184**	**14,337**	**15,543**	**16,658**
Retail Brand Management Costs	292	444	524	568	574	*1%*	700	714	729	743	758
Total Retail Profits before Indirect Overheads	**-290**	**181**	**2,189**	**4,868**	**7,894**	***7%***	**11,539**	**12,469**	**13,608**	**14,800**	**15,900**
Logistics Overheads	75	405	667	811	1,148	*1%*	1,401	1,429	1,457	1,635	1,516
Support Function Overheads	64	116	190	243	230	*0%*	280	429	437	297	303
Country Preoperating Expenses	131	154	0								
Total enterprise EBIT profit (before royalty)	**-372**	**470**	**3,713**	**7,869**	**12,257**	***11%***	**16,862**	**17,756**	**19,000**	**20,300**	**21,662**
Total Retail Profits before Interest & Tax (EBIT)	**-559**	**-495**	**1,332**	**3,813**	**6,516**	***6%***	**9,858**	**10,612**	**11,713**	**12,867**	**14,080**

Projected GCC system enterprise P&L statement (Scenario 10)

CURRENCY: **£ 000's**

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**3,744**	**19,307**	**47,609**	**81,119**	**114,824**	***100%***	**140,086**	**142,888**	**145,745**	**148,660**	**151,633**
Cost of Goods Sold	2,175	11,198	27,613	46,968	66,483	*58%*	81,110	82,732	84,386	86,074	87,796
Royalty on Sales	187	965	2,380	4,056	5,741	*5%*	7,004	7,144	7,287	7,433	7,582
Net margin	**1,382**	**7,144**	**17,615**	**30,095**	**42,600**	***37%***	**51,972**	**53,011**	**54,071**	**55,153**	**56,256**
Staff Costs	419	2,085	4,999	8,355	11,712	*10%*	13,588	13,717	13,992	14,420	14,860
Occupancy Costs	329	1,448	3,190	5,192	7,119	*6%*	8,265	8,430	8,599	8,771	9,098
Controllables	94	483	1,190	2,028	2,871	*3%*	3,502	3,572	3,644	3,717	3,791
Shrinkage	37	193	476	811	1,148	*1%*	1,401	1,429	1,457	1,487	1,516
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**257**	**1,687**	**4,760**	**8,599**	**12,487**	***11%***	**17,002**	**18,042**	**19,292**	**20,598**	**21,814**
Marketing Costs	150	772	1,904	3,245	4,593	*4%*	5,603	5,716	5,830	5,946	6,065
Operations Management Costs	150	521	762	892	919	*1%*	981	1,000	1,020	1,041	1,061
Total Brand Contribution	**-43**	**393**	**2,094**	**4,462**	**6,975**	***6%***	**10,418**	**11,326**	**12,442**	**13,611**	**14,687**
Retail Brand Management Costs	292	444	524	568	574	*1%*	700	714	729	743	758
Total Retail Profits before Indirect Overheads	**-335**	**-51**	**1,570**	**3,894**	**6,401**	***6%***	**9,718**	**10,612**	**11,713**	**12,867**	**13,929**
Logistics Overheads	75	405	667	811	1,148	*1%*	1,401	1,429	1,457	1,635	1,516
Support Function Overheads	64	116	190	243	230	*0%*	280	429	437	297	303
Country Preoperating Expenses	131	154	0								
Total enterprise EBIT profit (before royalty)	**-417**	**239**	**3,094**	**6,896**	**10,764**	***9%***	**15,041**	**15,898**	**17,106**	**18,368**	**19,691**
Total Retail Profits before Interest & Tax (EBIT)	**-604**	**-727**	**714**	**2,840**	**5,023**	***4%***	**8,037**	**8,754**	**9,818**	**10,935**	**12,109**

Projected GCC system enterprise P&L statement (Scenario 11)

CURRENCY: £ 000's

Year	1	2	3	4	5	%	6	7	8	9	10
Net Sales	**3,744**	**19,307**	**47,609**	**81,119**	**114,824**	***100%***	**140,086**	**142,888**	**145,745**	**148,660**	**151,633**
Cost of Goods Sold	2,175	11,198	27,613	46,968	66,483	*58%*	81,110	82,732	84,386	86,074	87,796
Royalty on Sales	225	1,158	2,857	4,867	6,889	*6%*	8,405	8,573	8,745	8,920	9,098
Net margin	**1,344**	**6,951**	**17,139**	**29,284**	**41,451**	***36%***	**50,571**	**51,583**	**52,614**	**53,666**	**54,740**
Staff Costs	419	2,085	4,999	8,355	11,712	*10%*	13,588	13,717	13,992	14,420	14,860
Occupancy Costs	329	1,448	3,190	5,192	7,119	*6%*	8,265	8,430	8,599	8,771	9,098
Controllables	94	483	1,190	2,028	2,871	*3%*	3,502	3,572	3,644	3,717	3,791
Shrinkage	37	193	476	811	1,148	*1%*	1,401	1,429	1,457	1,487	1,516
Depreciation & Amortization	245	1,248	3,000	5,110	7,263	*5%*	8,213	7,821	7,088	6,161	5,177
Store Contribution before Brand Costs	**219**	**1,494**	**4,284**	**7,788**	**11,338**	***10%***	**15,602**	**16,613**	**17,834**	**19,111**	**20,297**
Marketing Costs	150	772	1,904	3,245	4,593	*4%*	5,603	5,716	5,830	5,946	6,065
Operations Management Costs	150	521	762	892	919	*1%*	981	1,000	1,020	1,041	1,061
Total Brand Contribution	**-80**	**200**	**1,618**	**3,651**	**5,827**	***5%***	**9,018**	**9,897**	**10,984**	**12,124**	**13,171**
Retail Brand Management Costs	292	444	524	568	574	*1%*	700	714	729	743	758
Total Retail Profits before Indirect Overheads	**-372**	**-244**	**1,094**	**3,083**	**5,253**	***5%***	**8,317**	**9,183**	**10,256**	**11,381**	**12,412**
Logistics Overheads	75	405	667	811	1,148	*1%*	1,401	1,429	1,457	1,635	1,516
Support Function Overheads	64	116	190	243	230	*0%*	280	429	437	297	303
Country Preoperating Expenses	131	154	0								
Total enterprise EBIT profit (before royalty)	**-417**	**239**	**3,094**	**6,896**	**10,764**	***9%***	**15,041**	**15,898**	**17,106**	**18,368**	**19,691**
Total Retail Profits before Interest & Tax (EBIT)	**-642**	**-920**	**237**	**2,028**	**3,875**	***3%***	**6,636**	**7,325**	**8,361**	**9,448**	**10,593**