OPPORTUNITIES AND THREATS REGARDING THE DEVELOPMENT OF THE FRANCHISING BUSINESS MODEL IN CROATIA

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1. INTRODUCTION

Franchising as a way of doing business is often used in economically developed countries, and its use has grown dramatically over the last two decades in both the USA and Europe (Alon & McKee, 1999). A 2004 study of franchising's economic impact conducted by The International Franchise Association showed that the franchise market in the USA generates over $1.4 trillion (i.e., over 45% of total retail sales) with 18.6 million people directly and indirectly employed (IFA, 2004). Research conducted by the European Franchise Federation in 2004 indicated that there were more than 5,500 franchisors and more than 266,000 franchise locations in Europe (EFF, 2004). According to the same research, the USA and Asia have around 4,000 franchisors each.

Franchising as a way of doing business is suitable for two types of companies:

- Those that want to "grow" in a geographical sense and not rely exclusively on their own financial resources. These companies become franchisors and sell the rights-of-use of their established brand names and developed know-how to local companies in targeted areas;

- Those that want to enter certain industries but as a part of bigger systems. These companies become franchisees and buy rights to use established brand names and to use established models for ways of doing business in certain business fields.

The franchising literature indicates the numerous advantages, disadvantages and challenges of franchising from both the franchisor and franchisee points of view. However, there is limited evidence about the status of franchising in Croatia regarding the number of Croatian companies which are part of international franchising networks and the number of Croatian companies which became franchisors together with results of their business.

The present paper discusses issues related to the implementation of franchising business models in Croatian companies, using The San Francisco Coffee House as a referential case. The paper investigates the potentials, barriers and significances of adapting franchising concepts on a microeconomic level.

This study explores the condition of franchising in Croatia, aims to contribute to the body of evidence about Croatian franchising, and contributes to theoretical research on international franchising. Therefore, a number of the stakeholders will benefit from this investigation: managers, investors, potential entrepreneurs, service providers (financiers and advisors), policy makers, and theoretical researchers.

2. BACKGROUND

2.1. Franchising - origin and definitions

The word “franchise” comes from the Norman French word "fraunchise," which was derived from the French word "frank" – free man, free to work something.[1] The English word "franchise" originally was used to describe liberation from any prohibition, permission, or privilege – by which a company is allowed to do or not to do something for which it would normally not have rights.

Franchising is a privilege or allowed right given to an individual or group that allows recipients to do certain commercial activities. It is a way of widening a given business’s field, including the right to distribute products and services under a better-known brand name. Franchising can be divided into two main types: product/trade-name franchising and business format franchising. According to Falbe & Dandrige (Alon, 2006, p. 43), product/trade-name franchising is a distribution system in which suppliers make contracts with dealers to buy or sell products or product lines. Business format franchising is a continuing relationship in which the franchisor provides a licensed privilege to do business—plus assistance in organizing, training, merchandising and management—in return for a consideration from the franchisee (Alon, 2006, p. 12). In other words, a franchise occurs when someone develops a business model and then sells the rights for doing business under that model to another entrepreneur, the franchisee. The entrepreneur who sells the rights is the franchisor. The franchisee generally gets the rights to the business model for a certain period and within a certain territory.

2.2. Franchising’s advantages and disadvantages

As in any potential business arrangement, the sides involved need to ask questions about the advantages and disadvantages of the nascent relationship. There are numerous advantages for those entrepreneurs who choose franchising as a growth option: Murray (2003, p. 15) has emphasized faster growth, the development of better managerial skills, and benefits that

[1] The Random House Dictionary of English Language, Random House, New York, 1973. (*The word frank comes from the word "Frank," which described members of German tribes who lived in Gallia in the 5th century C.E.. In Gallia, which was under the Francs, only they – invaders – had full freedom as well as the ones who were under their protection. In old European law there was an expression "Francus homo" which was describing free citizens)*

accrue from local knowledge. Other advantages include minimizing business and financial risks to the franchisor, fewer employees in the field and less administration in the main office(s), and the faster establishment of a national image for the company - because of franchise-system growth. As a result, the challenges associated with competition are diminished.

Parivodić (2003, p. 54), states that the biggest disadvantage for a franchisor is the potential loss of the control over the franchise network. Murray (2003, p. 17) states further disadvantages specific to the franchisor: the dangers of franchisees not sticking to the franchisor's standards, the potential for a less profitable business, potential conflicts with franchisees, and lack of trust between the parties. Since the employees have the biggest role in a given franchise's potential for success, another disadvantage is related to the fact that the franchisor cannot influence the franchisee's hiring policies, though some franchisors do mandate (or try to mandate) training and adherence to certain work rules throughout the franchise network.

The franchise relationship would not develop if a potential franchisee did not see advantages to conducting business using a field-tested business recipe and under the known name of the franchisor. Some of the advantages for entering the franchise network from the franchisee's point of view are overcoming shortfalls of knowledge and experience compensated for by training provided by the franchisor, using a successful and established business name and reputation, retaining a certain level of independence as an entrepreneur, and realizing the group benefits of economies of scale (Spasić, 2006, p. 28).

Other authors note additional advantages: lower risk of failure, standardization of product and quality, help in choosing location(s) and other logistical activities, benefits from the franchisor's research and marketing program(s), and some protection from competition.

Thomas and Seid (2000, p. 39) have observed significant disadvantages for franchisees: lowered independence, greater addiction to franchisor's non-elastic franchise system, and unrealistic profit expectations. For some franchisees, an additional disadvantage is the obligatory, continuous coordination of contracts and standards that are prescribed by the franchisor and the franchise system, including those financial obligations which the franchisee has to pay regardless of his actual financial status.

3. ENVIRONMENTAL ANALYSIS OF FRANCHISING IN CROATIA

3.1. The Economic Environment of Franchising

In the beginning of the 1990s, after The Republic of Croatia gained its independence, the Croatian market opened to a great variety of international products and services. Due to the economic growth which began in the late 1990s, salaries have grown appreciably, especially in the larger cities and in certain other parts of Croatia (DZS, 2006). Salary growth resulted in increased consumer demand for higher-quality world brand names, which were not widely available in Croatia at that time. After independence, the Croatian market became flooded with imported goods of variable quality. The habits of younger Croatian consumers, according to a study conducted by GfK Croatia (2005), changed as a result of this increased supply: international brands became the acquisition target of younger consumers, while older people tended to continue to seek out domestic brands. Inevitably, perhaps, purchasing habits also varied geographically.

Financial institutions in Croatia are mostly owned by foreign banks – around 90% according to HNB (2006) – and many of these acquisitions have occurred in the last few years. Although there are a predictable variety of capitalization options for would-be entrepreneurs, a main characteristic of the Croatian domestic market is the bankruptcy of small entrepreneurs as they struggle to collect their own debts. Although barter is a common fixture of the domestic market (between local companies, i.e.), the international ownership of local banks makes such traditional arrangements problematic.

Creating a vibrant business environment in accordance with the standards of the European Union and with countries embedded in the local market economy is one of the major goals of the Croatian government’s economic policies. The Government’s dedication to the reform of the national economy can be seen in its desire to attract foreign investment for the development of Croatia’s domestic and international markets.

Foreign investments in Croatia are regulated by the Company Act and other legal norms. A foreign investor in Croatia has a number of organizational options available to him or her according to this Act: a foreign investor can invest alone or as a joint-venture partner with a Croatian company or private citizen; there are no constraints as to the percentage of foreign ownership that is possible. In addition, in keeping with the Government’s desire for foreign investment, investors can gain access to a number of newly opened markets; entrants can take advantage of a number of incentives, tax benefits and customs privileges that are only available to foreign investors.

3.2. The Institutional Environment of Franchising

Since the concept of franchising is relatively new to Croatia and its inhabitants, it is necessary to stimulate and incentives franchising relationships. Presently (2006), there are two Centers for Franchising in Osijek and Zagreb. Each works with the Croatian Franchising Association to stimulate franchising development in several ways:

- Educating about franchising – The Franchise Center in Osijek is organizing seminars, "Franchise A to Z," in order to educate entrepreneurs about franchising and its benefits;

- Franchising promotion – both Centers and the Association are trying to promote franchising as a way of doing business through local media – interviews, articles in the newspapers and magazines, et al.;

- Creating websites with information about franchising on the Internet – information on the portal with current news;

- Connecting supply and demand between franchisors and potential franchisees – one section of the franchise portal contains offers from franchisors interested in the Croatian market; there are several inquiries each week from potential franchisees;

- Helping domestic companies to become franchisors – The Franchise Center in Osijek, with the help of Poduzetna Hrvatska, organized training for potential franchise consultants who can help domestic companies if they decide to use franchising as a growth strategy;

- Establishing franchise fairs and round tables.

Foreign franchises tend to choose one of two potential pathways into the Croatian market: distribution-product franchising and/or business-format franchising. Larger, better-known franchisors like McDonald's open their offices in Croatia and offer franchises to interested entrepreneurs in order to ensure quality control, while smaller and less-well-known franchisors sell master franchises to local entrepreneurs in order to ensure the benefits of local knowledge and cost savings.

During the last few years, The Republic of Croatia has approved a number of laws which resulted in Croatia's acceptance into the World Trade Organization, CEFTA (Central European Free Trade Agreement); these legal changes have also allowed Croatia to begin negotiations for acceptance into the EU. Nevertheless, there is no specific legal basis for franchising in Croatia. Franchising is mentioned in Croatian trade law (Narodne Novine, 2003), where the generalities of potential franchising agreements are stated, but mention is made in only one article and that mention is very condensed. Therefore, there is no legal standard for the development of franchising and no legal parameters (yet) for franchising agreements: at the present time, business practices on the ground determine the appropriateness of such agreements.

3.3. The Current State of Franchising in Croatia

The first franchise appearance in the Croatian market was credit-card franchisor Diners Club International, which entered the market in 1969. "When the former Yugoslavia collapsed, the Zagreb-based office that had been in existence since 1969 signed a franchising agreement with Diners Club which allowed it to operate under license within both the former Yugoslavia and other Balkan countries."[2] For its successful performance in the Eastern European market, Croatian franchisee Diners Club Adriatic won two awards from its Chicago based franchisor.

Franchises became more the norm in Croatia starting in the early 1990s, when the first McDonald's was opened in Zagreb. "McDonald's expansion into the Croatian market has tended to use two franchising methods: direct franchising and business-facility lease arrangements… Such lease arrangements allow for franchisees to become entry-level franchisees using less capital at the outset."[3]

Other franchisors followed McDonald's lead. One of the relatively new franchising concepts in the Croatian market is the Hungarian company Fornetti, which managed to spread quickly its mini-bakeries business throughout Croatia by using franchising. They were founded in 1997, and today have more than 3000 locations in Central and Eastern Europe (Mandel, 2004). Other international franchises represented in Croatia include Benetton, Subway, Dama Service, and ReMaX.

3.3.1. Data and Trends

Franchising as a business model is still in development in Croatia. In relation to other countries in transition, other emerging markets, Croatia is in the middle of the pack with 126

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[2] Viducic, Lj., Brcic, G. In Alon, Il; Welsh, D. (2001) International Franchising in Emerging Markets: China, India and Other Asian Countries», CCH Inc., Chicago, p.218.

[3] Viducic, Lj., Brcic, G. In Alon, Il; Welsh, D. (2001) International Franchising in Emerging Markets: China, India and Other Asian Countries», CCH Inc., Chicago, p.217.

franchise systems. According to data supplied by the European Franchise Federation, Hungary leads the way with around 300 systems, of which 50% are domestic. Poland trails Hungary with 210 franchise systems (55.7% domestic). Croatia is, as of 2006, ahead of the Czech Republic, which has 90 franchise systems. Trailing Croatia are Bosnia and Herzegovina, Serbia, Montenegro and Macedonia. Slovenia has around 100 franchise systems, although this is a much smaller market. However, the number of franchise systems in Croatia has increased in just the last two years. According to the Croatian Franchise Association, there are approximately 125 (25 of them domestic) franchise systems present in the Croatian market. These systems operate approximately 900 locations and employ almost 16,000 people (Kukec, 2006)

Franchisors in more than 20 industries have chosen franchising as a growth option, with the sales industry and fast-food sectors accounting for more than 20% of the market (Kukec, 2006). Other segments with important shares include the tourist industry, rent-a-car companies, courier services and the fashion industry. The newest franchise systems are being started in a variety of service-sector industries.

Tables 1 and 2 show the most well-known foreign and domestic franchisors in Croatia by industry and number of outlets as of 2007:

Table 1: Foreign franchisors in Croatia

Franchisor	Industry	Number of outlets
McDonald's	Fast food	16 restaurants
Subway	Fast food	6 restaurants
Fornetti	Bakeries	Over 150 locations
Dama service	Refilling toner cartridges	3 locations
Berlitz	Foreign language school	1 location
Firurella	Weight loss center for women	2 locations
Berghoff	Kitchen equipment	3 locations

Source: Round table – Franchising in Croatia EFF/IFA International Symposium, October 24-25, 2006, Brussels

Table 2: Domestic franchisors in Croatia

Franchisor	Industry	Number of outlets
Elektromaterijal	Household appliances’ distribution	Over 50 stores
X-nation	Fashion clothes	40 stores / corners
Rubelj Grill	Grill	17 restaurants
Skandal	Fashion clothes	15 stores
Body Creator	Weight loss center for women	4 centers
Bio & Bio	Health food	3 shops
Bike Express	Courier service	1 location
San Francisco Coffee House	Coffee bar	2 locations

Source: Round table – Franchising in Croatia EFF/IFA International Symposium, October 24-25, 2006, Brussels

3.3.2. Barriers to the Development of Franchising in Croatia

During September 2006, The Franchise Center of the Center for Entrepreneurship in Osijek conducted a survey of 50 people, asking what examinees (representatives of banks, entrepreneurs, and lawyers) thought about the barriers facing franchising in the Croatian. Their responses included:

- Laws – there is no legal regulation of franchising in Croatia. The word "franchising" is only mentioned in Trade Law. But, Croatia is not unusual in this respect: only 52 countries in the world mention franchising in any significant way in their legal systems (Zeidman, P.F , 2006). Common or no, however, the absence of clear legal precedent makes it difficult for Croatian lawyers to help their clients, especially during the contracting phase—whether franchisor or franchisee, whether foreign or domestic investor.

- Infrastructure – there is a dearth of infrastructure related to franchising: no banks that will assist franchisors or franchisees, too few educational centers, no franchise consultants who could help potential franchisors in developing their own networks. Banks seem unable to distinguish between start-up entrepreneurs creating footholds in new franchise sectors and franchisees who are entering preexisting, proven franchise systems. There is not enough education about franchising, so even potential franchisors and franchisees do not know where to go to and who to contact if they would like to find more about franchising and how it can work.

- Problems with banks (not familiar with franchising) – banks do not recognize franchising as a relatively safe way of entering into a new business and do not have any specialized loans for the franchising industry. According to a survey conducted by the Franchise Center (2006), some banks' representatives said that they would ask a guarantee for a loan from the franchisor also. Banks are not willing to educate their employees in order to learn about this way of doing business.

- Small market – because there are only 4.5 million inhabitants in Croatia, examinees are pessimistic that the largest franchisors will come to Croatia due to logistical problems: the perception is that it is much easier to open a location in London than in Croatia. Large and famous franchisors are looking on bigger area in sense of population number_developing new franchises, and they often resist adapting to local standards and prices. Smaller franchisors that would like enter to Croatia are not as well known to Croatian entrepreneurs and are therefore seldom franchisors of choice.

- Franchising is not a well-known way of doing business – people seldom recognize what franchising is; many think it is connected with insurance. This is the biggest barrier according to the survey because people are not willing to enter into something with which they are unfamiliar. Further seminars and round tables need to be organized in order to educate entrepreneurs about franchising and its potentials and benefits.

Examinees also report that there is an excellent chance for franchising in Croatia, that there is the possibility of high growth in this sector (up to 30%), and that Croatia's membership in the EU will provide the necessary boost to development. This survey showed that although franchising is not a familiar way of doing business, examinees see a bright future for franchising in Croatia.

According to the above-mentioned survey, there are some identifiable reasons for the relatively slow development of franchising in The Republic of Croatia: entrepreneurial thinking, lack of franchising education, and a weak national franchising association. First, many entrepreneurs would rather own their own companies and have complete "business freedom" than submit to the restrictions they see as related to becoming part of a system – from production and distribution to sales and cleaning of the premises. Second, Croatian entrepreneurs are not completely familiar with the benefits which can be gained by being a member of a successful franchising system.

Both barriers to franchising growth can be overcome by establishing an education system and governmental/financial support for this potentially vibrant business sector.

4. DEVELOPING A FRANCHISING SYSTEM IN CROATIA – THE CASE OF SAN FRANCISCO COFFEE HOUSE

4.1. Background

In the spring 2004, after spending 6 years in the USA, husband-and-wife team Jasmina Pacek and Denis Tenšek returned to Croatia. During their stay in the USA they had gained significant business experience.

Jasmina had worked for several companies: AVL – a company that works with programs for computer design; Northcoast Industries – a fashion store in San Francisco where she started as designer and was promoted to Art Director; and finally Keeco Corporation, which is a leader in house-textile products in the American market. At the same time, Jasmina finished her MFA in Fine Arts and Design at the University of California, where she worked for some time as a teaching assistant. Denis finished his MBA in Business Management at California State University. From 1998 until 2004, he worked in two companies: Tyco Inc. and Brinks Home Security as regional manager. For personal reasons, Jasmina and Denis decided to return to Croatia, to Osijek, where Jasmina's parents were living. Thanks to successful careers and wise investments in real estate in the USA, they returned to Croatia with enough capital to help them in their new start.

After they spent some time in Osijek, they decided to start a new business. While thinking about what they should do, they had noticed that there were many coffee bars in Osijek and that visiting them was part of the life style of the local population. However, all these "bars" offered the same limited product line; they noticed that what was missing in the market was an American-style coffee bar in which most of the offerings would consist of different types of coffee and include the novel (in Croatia) possibility of getting "coffee to go." They decided to adapt this ubiquitous American concept to the local Croatian market. Convinced that the "Made in USA" brand would be positively received in their new market, they named the coffee bar "The San Francisco Coffee House." Jasmina designed a visual identity for their coffee bar, and Denis went about finding proper suppliers of raw materials and finalizing the financial side of the whole project. During the development of the business plan, he traveled several times to the USA, bringing back suitcases full of coffee mugs, pictures, newspapers, and ideas related to décor.

4.2. Opening of The San Francisco Coffee House in Osijek

They had chosen the location for The San Francisco Coffee House very carefully: They were looking for a location with a minimum of 80 square meters near an area with heavy foot traffic, since their main target market was to be business people. They found an excellent location in the town's center – across from the green market, near three University departments, several lawyers and public notaries' offices – for which they signed a 3-year lease with provisions for extending the lease and a right to pre-emptive purchase in case the owner wanted to sell the premise. After the first few months, they found that their major client markets were students and business people, mainly female in both cases.

The San Francisco Coffee House offers its customers coffee in 17 different latte (with milk) and mocha variants and American-style muffins in several varieties. Coffee can be taken in the pleasant atmosphere of the bar or it can be taken out in “to-go" packaging. In order to adapt to their target market, guests are provided Croatian and foreign newspapers and magazines, have free wireless access to the Internet; the ambience is enhanced by smooth jazz and foreign music from the 70s and 80s.

Today there are 8 employees in SFCH[4], which is managed by Tanja Škaro. The employees are all young people, all without any previous working experience and all of whom have worked in SFCH from its inception. When searching for employees, Jasmina and Denis looked for trustworthy, loyal and honest people. For each workstation, employees have a detailed job description and detailed checklists for each shift and for weekly and monthly routine duties. After employment, all employees passed education for working in bar and their salaries are almost 20% higher those of comparable employees at other local coffee shops.

4.3. SFCH – Creating the Franchise Offer

From the beginning, Jasmina and Denis believed in the success of their idea and in its potential for further growth. Osijek is center of Osijek-Baranja County, which is among the least developed in Croatia[5]. Profitability in this area could be repeated in almost any other location in Croatia. They were sure about this.

Jasmina and Denis talked several times about expanding SFCH by franchising. After they established SFCH, they decided to talk about this idea with consultants from The Franchise Center of The Center for Entrepreneurship in Osijek, which was offering seminars on franchising to entrepreneurs according to the "recipe" bought from the Center for Franchising at The University of Texas, El Paso. Consultants at the Center had a lot of information about franchising and some useful contacts, but they had no practical experience developing franchise networks using existing Croatian companies.

When thinking about the growth of their business, Jasmina and Denis did not want to invest their own money opening other locations in Croatia. Taking advantage of one of franchising’s most attractive options, they saw potential in attracting financial investments from franchisees, dedicating themselves to the "core" business while transferring operational business activities in satellite locations to franchisees.

Developing the SFCH franchise was a project that allowed Jasmina, Denis and The Franchise Center to learn together. Since they did not yet have potential investors and had no anticipated time for return on their own investment in franchise development, they tried to lower the cost of franchise entry as much as possible.

One of the first steps they took was to register and protect the name and logo of SFCH, for which Jasmina – instead of hiring a lawyer who specialized in intellectual property rights

[4] SFCH – short from for The San Francisco Coffee House.
[5] Singer et al., (2005), Strategija razvoja Osječko-baranjske županije, page 85

protection – studied documents and application papers. She did everything on her own and paid only one-third of the costs a lawyer would have charged.

An SFCH franchise offering resulted from the teamwork of Jasmina, Denis and The Franchise Center. They found key elements for the franchise offer they would craft in different ways: by reading franchise literature, by analyzing the franchise offers of competitive companies, and finally by always returning to the SFCH to assure themselves of reliability of concept. They wanted to build a concept which would be not only attractive to the investors, but which would also ensure them a reasonable return on their investments in the development of the franchise even as resources could be allocated to the further development of the core business, quality improvement of the business model, and increasing brand awareness at the national level.

The SCFH franchise offering was the result of several months of work and research: it was intended for towns with more than 40,000 inhabitants or to tourist areas where the native population was quite a bit lower. Franchisees in towns with fewer than 40,000 inhabitants would have territorial exclusivity; in larger towns this could be negotiated. The location of the coffee bar had to be in a town center, near commercial walking zones, shopping centers or similar high-traffic pedestrian areas. Concerning investment level and location size, four models of SFCH franchises were proposed: *beginner, standard, professional & world class.* The level of initial investment in relation to the franchise model varied from €7,000 to €45,000. Monthly royalties paid to the franchisor would range from €50 to €200, depending on the level of the franchise model and the level-of-use of default suppliers for three major raw materials: coffee, flavorings and packaging for "coffee to go." Franchisees were required to use designated suppliers so that the franchisor could control the quality of the product, though not the operations of the independent franchisee. In order to have good franchise-relationship functionality, the franchisor had to have an interest in the franchisee business, which is in the SFCH case based on the rebate system for raw materials since the franchisor is the only supplier to the franchisees.

The franchise package includes education on three levels: the franchisee, the manager, and the servers in the coffee bar. In addition, the franchisor provides initial marketing support to the franchisee by establishing contacts with local and national media and helping franchisees with opening their stores. The initial franchise contract for SFCH is for 5 years with the possibility of prolonging the contract after that period.

4.4. SFCH - Concept Sales

With a developed franchise offer and clear expectations for potential SFCH franchisees in place, Jasmina and Denis started their search for entrepreneurs who would recognize a good idea and its profit potential. During this search, they were trying to minimize their own expenses, so they decided to use a guerilla-marketing approach even as they availed themselves of The Franchise Center in Osijek and the Entrepreneurial Franchise Center Promaturo in Zagreb. In the event that either of the Centers found a franchisee who would sign a franchise contract, that Center would receive certain percentage of the franchise fee as a finders' fee. Jasmina and Denis realized that they did not really have any other choices for attracting franchisees because of franchising's relative invisibility in Croatia. They realized that it would be necessary to educate potential investors about franchising, that it would not be enough just to offer the SFCH concept to the public.

Jasmina and Denis have received a number of inquiries from entrepreneurs throughout Croatia. They have met with several potential franchisees who were extremely interested in their concept; however, even though these were good candidates, they seldom had the necessary financial resources. While trying to aid their would-be franchisees, the couple discovered that there were no specialized financial products on the market for start-up entrepreneurs who wished to become franchisees. Moreover, they found out that the banks had not yet recognized the lower risks of investment associated with start-up entrepreneurs would wished to become franchisees rather than independent business owners.

In September of 2006, The Franchise Center of the Center for Entrepreneurship in Osijek with financial assistance from USAID project "Poduzetna Hrvatska" and with the help of American consultant for franchise business Ilan Alon, Ph.D., held a seminar on franchising for bank representatives. According to research done on a sample of 7 banks,[6] a majority of banks' representatives were aware that there are no adequate specialized financial products for potential franchisees. Bankers explained this inadequacy by stating that there was not enough demand for this type of financial product and that there was no legal basis which would make franchising a safe investment in Croatia. The absence of adequate avenues for financing franchisees inevitably limited the market of potential SFCH franchisees.

4.5. SFCH – First Franchisee

One of the interested franchise candidates with whom Denis had spoken by telephone came one day by car from the Croatian town of Split, almost 700 km away, in order to see the SFCH operation for him. After a whole day of discussion about the business and the potential development of SFCH, Tomislav Kuzmanić went back to Split and, after a few weeks, invited Jasmina and Denis to visit him and to evaluate several potential locations for an SFCH franchise in Split. Jasmina, Denis and Tanja – the coffee bar manager in Osijek and future coordinator of the franchise network – visited locations in Split which Tomislav proposed; they ultimately chose one for which Tomislav soon signed a 5-year contract as a franchisee. The location is in the old part of Split, near the Diocletian palace; it is even larger than the coffee bar in Osijek.

Signing this first franchisee meant also finalizing the version of a franchise contract for all future SFCH franchises. Jasmina and Denis had only completed a draft version of the contract, which they had planned to adapt to the specifics of the situation once they located their first franchisee. Since there are no lawyers who specialize in franchising contracts in Osijek and only a very few, all with very limited experience, in Croatia as a whole, they decided to hire Margareta Krivić, a young lawyer and Denis's former schoolmate. From the start, Margareta showed great interest, effort and willingness to learn with them as she investigated this new area of the law. Jasmina and Denis thought that Margareta's dedication and determination would more than compensate for her inexperience, especially given the paucity of legal precedent related to franchising in Croatia. Too well aware of the disordered legal system in Croatia when it came to the franchising and to functional problems in the legal system in general, Denis, Jasmina and Margareta devoted a great deal of time on this first franchise contract so that all parties would have their interests protected.

[6] Representatives of following banks attended seminar: Privredna banka Zagreb d.d., Erste & Steiermarkische bank d.d., Zagrebačka banka d.d., NOA – štedno kreditna zadruga, Varaždinska banka d.d., Hrvatska banka za obnovu i razvoj i Slatinska banka d.d..

At the same time, while they were finalizing arrangements with the franchisee from Split, Jasmina and Denis used the offices of The Franchise Center in Osijek to get in contact with several young entrepreneurs from Zagreb. They were interested in opening an SFCH franchise in Zagreb, and they were currently looking for a suitable location for what would be the second SFCH franchise. According to Denis's and Jasmina's estimation, Zagreb could profitably accommodate several SFCH franchises based on the number of its inhabitants.

CONCLUSION

Franchising is one of several possible models for business growth and is widely used in economically developed countries throughout the world. Some of the reasons why companies prefer to develop franchise networks rather than creating subsidiaries include lower financial investment, lower risk, faster growth, and local market knowledge by franchisee; and the franchisee's motivation to succeed.

There are few franchisors in Croatia in relation to its neighboring countries although franchising's possibilities are quite numerous. The barriers which the San Francisco Coffee House faced during its development of a franchise network highlight the major challenges which face Croatian companies as they seek to establish their own networks. In sum:

- There is just not enough information about franchising. As a result, entrepreneurial and institutional awareness of franchising is quite low;

- There are no well-established support organizations for the development of franchise networks in Croatia. There are only two Entrepreneurship Centers in Croatia which offer services regarding franchise network development;

- There is no legal regulation of franchising. At the present time, there are no standards for franchising contracts, and there are not enough lawyers familiar with franchising;

- There is no significant support from financial institutions. Banks fail to recognize the relatively lower risk of investment in start-up entrepreneurs/franchisees than in independent start-up entrepreneurs.

At this time, companies in Croatia that decide to develop their own franchise networks should be aware of additional challenges they will face during that developmental process.

The present research is preliminary and exploratory. It is based on an analysis of one exemplary case that underlines several significant issues, but this should be followed by research on larger samples using a quantitative rather than a qualitative approach.

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