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RESEARCH ARTICLE

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# A Study on the Key Factors Influencing International Franchisors' Choice of Entry Modes into China

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**Abstract** This paper examines factors associated with international franchising firms' entry modes when they enter the Chinese market. To this end, a survey was conducted to investigate the linkage between entry modes and characteristics of franchising firms. The logit model and regression analysis were used to test the hypotheses. Findings reveal four factors that significantly influence international franchisors' entry mode choices including cultural and geographic distance, international market experience, risk spreading, and maturity of the franchising system.

**Keywords** Chinese market, international franchising, direct international franchising, entry modes

## 1 Introduction

The choice of market entry mode is an essential issue in a firm's internationalization. Identification of influencing factors in relation to firms' entry mode

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choice has been intensively studied in the extant literature. However, although there is much literature examining the relationship between key influencing factors and international franchising entry modes choice, few studies have investigated international franchisors' choice of entry modes when entering the Asian emerging markets, especially China.

Emerging economies account for 80% of the world's population and 60% of the world's natural resources. They offer the greatest potential for long-term growth to international companies, including franchising companies (Welsh and Alon, 2001). China is one of the largest emerging economies with tremendous market potential (Sinclair and Xiong, 2006). Since the economic reform policy initiated by Deng Xiaoping in 1978, China has increasingly attracted the attention of foreign investment. By 2006, there were more than 570 000 foreign-invested firms in China (Song, 2006).

One of the emerging streams of literature focuses on the choice of entry mode by firms when entering international markets. Examining foreign businesses operations in China, international franchising has become one of the key market strategies for foreign firms entering the Chinese market, especially the franchising companies from the United States. Despite being a well-known business model in Western countries, franchising as a business mode had not been recognized by Chinese people until the 1980s, due to the rapid expansion of American franchising companies in China (Wang et al., 2008). Nevertheless, it has become a fast growing area in China. According to the China Chain Store and Franchise Association (CCFA, 2007), the total number of franchising systems in China (including domestic franchising systems) has currently reached 2 620 with an annual increase of 10.5%. The total number of outlets now has reached 168 000, with a total annual turnover of more than 25 billion dollars. It provides 2.4 million jobs, with a 53% annual growth rate (CCFA, 2006). Although China has become a global leader in terms of the number of franchise systems, each system in China averages only 72 outlets, which is much lower than the average of 540 outlets per system in the United States. Sales revenue from franchise systems accounts for only 3% of total retail sales in China, compared with an average of 40% in developed markets (CCFA, 2006). Thus, in spite of the rapid growth of China's franchise sector, it is still in its infancy (Sinclair and Xiong, 2006). CCFA's statistics indicate that there are about 500 international franchising systems in China, including 70% of the top 20 American franchising giants. Experts estimate that at least another 2 000 international franchisors are planning to enter into the Chinese market in the near future (CCFA, 2006).

This research has implications for both policy makers and international franchising practitioners. For the policy makers in the host countries, they can tailor their support to attract international franchisors. In addition, the findings of

this study provide guidance to practitioners in selecting franchising entry modes effectively. This study not only extends the mainstream theory of international franchising in the context of Chinese market, but also provides timely information on the current status of international franchisors in the Chinese market.

This paper consists of five sections. Next, there is a literature review of relevant theories, followed by hypothesis development. Section 3 describes the research methods. After presenting main findings and discussions in Section 4, conclusions are drawn and practical implications are discussed.

## 2 Literature Review

Operating in emerging markets has both advantages and disadvantages for international franchising firms (Elango, 2007; Welsh, Alon and Falbe, 2006). The choice of entry mode is one of the most important decisions for an international company (Anderson and Gatignon, 1986; Root, 1987). Nair (2001) suggested that franchising companies entering into China can choose either direct international franchising or other entry modes. In the former case, franchisor grants franchise rights to franchisees in China. Nair (2001) further pointed out that difficulties may arise by adopting franchising due to the unique characteristics of the business environment in China. The advantages and disadvantages of alternative entry modes and factors considered by franchisors have been previously analyzed through theoretical development and empirical studies (Konigsberg, 1991). However, how different factors influence international franchisors' entry mode choices have not been fully studied, especially in the context of developing countries like China. Attempting to fill the research gap, this paper intends to empirically examine the key factors affecting international franchisors' choice of entry modes into China.

Jensen and Meckling (1976) defined entry mode as the institutional arrangement by which a firm gets its products, technologies, human skills, or other resources into a market. In the context of internationalization, markets here usually refer to foreign markets. Selecting suitable entry mode is a central issue when a firm considers expanding its business internationally. Young, Hood and Hamill (1988) recognized that firms can select from a wide range of alternative market entry modes and the influencing factors can be divided into external factors and internal factors (e.g., firms' international experience, and its attitude to risk spreading).

### 2.1 External Factors

Environmental factors are highly significant to international franchisors in

choosing a host country for expansion (Alon and McKee, 1999). Previous studies have confirmed the value of country-specific factors (Dunning, 1988; Brouthers, Lance and Werner, 1996). Goodnow and Hansz (1971), and suggested that the extent of investment as well as the degree of control exercised by parent firms over distribution channels in other countries is related to the host country's environment, with the extent of investment and degree of control declining as the environment becomes less favorable (Goodnow and Hansz, 1971). They concluded that external factors not only influence the choice of distribution, but also influence whether a firm chooses to enter a market. Osland and Cavusgil (1996) proposed that these two factors are influenced by host-country-specific factors and industry factors. Host-country-specific factors include country risks and location familiarity (Hill, Hwang and Kim, 1990). Important distance factors in location familiarity include physical and cultural distance (Eroglu, 1992). Physical distance is one of the most frequently mentioned factors in the U.S. international franchising expansion. Cultural distance refers to the differences between the culture and language of the host and home countries. Cultural differences between the franchisor's home country and host country, particularly with regard to values and methods, can create internal uncertainty as well as problems in business conduct (Anderson and Gatigon, 1986). Studies have confirmed that national culture gap, particularly that between western culture and eastern culture, strongly affects a firm's management and business activities abroad (Hofstede 1980; Tes and Pan, 1997; Taylor, Zhou and Gregory, 2000; Koch, 2001).

Tes and Pan (1997) concluded that two culture dimensions (i.e., power distance and uncertainty avoidance) greatly affect the choices of market entry mode. They stated that firms with a more distant culture prefer an equity-based entry mode while firms from countries characterized by lower uncertainty avoidance culture are more likely to choose low cost entry modes to avoid risks. Since the East Asian society has different institutional structures from that of western societies (Taylor, Zhou and Gregory, 2000), when East Asian firms enter into overseas markets, the cultural gap is a significant factor affecting their choice of market entry modes. One good example is the Chinese *guanxi* culture (network of personal connections). *Guanxi* is embodied in friendship and affection. In the context of Chinese business, with a strong *guanxi* network among powerful persons or government, international firms from the Western societies are more willing to take risks. In other words, they will choose a high level control entry mode. Social cultural distance between home country and host county discourages companies from choosing a wholly-owned entry mode (Sun, 1999). The differences in management orientation naturally following from cultural differences have also been addressed by previous studies (Jagersma and Gorp, 2003; Hofstede, 1980).

Accordingly, we develop the first hypothesis as follows:

**H1** The greater the cultural and geographical distance between China (as the host country) and the home country of a franchisor, the less likely a franchisor to adopt direct international franchising as its entry mode into China.

## 2.2 International Business Experience

International business experience has been recognized as an important factor affecting an international franchising firm's choice of entry mode. Franchising firms like McDonald's would like to use their rich experience to develop business in similar markets. Shama (1995) found that the relatively positive experience of the U.S. companies aiming to enter foreign markets has played a very important role in developing eastern European countries. Several empirical studies have found that international experience significantly affects a firm's choice of entry mode. Anderson and Gatignon (1986) argued that a firm's international experience is positively related to firms choosing the high-level control mode. The more international experience a firm has, the more likely it to adopt a higher level of control. This finding has been supported by Herrman and Datta (2002). Whitelock (2002) also postulated that international experiential knowledge is a significant factor in international marketing. Direct international franchising gives less control compared to other entry modes, such as joint venture (Sun, 1999).

Hence,

**H2** The more the international franchising experience of a franchisor, the more likely it is to adopt direct international franchising as its entry mode into China.

## 2.3 International Franchising System Life Cycle

Once a franchising system reaches its maturity stage at the home country, it often begins to explore international markets (Jahanson and Vahlne, 1990). Carney and Gedajlovic (1991) developed a path model of the franchising life cycle that incorporates resource scarcity theories and agency theories. Similar findings were reported by Lafontaine (1992): She found that franchising is prevalent when there are incentive problems, but firms also use franchising to accelerate their expansion. Lillis, Narayana, and Gilman (1976) divided the franchising system life cycle into four stages, namely penetration, growth, maturity and late maturity. Based on franchisers' operation years and outlet number, stages of international franchising system can be classified as follows (Table 1):

**Table 1** Franchising Life Cycle

| Stage | Operation years | Outlet number |
|---|---|---|
| Penetration | 0–5 | 0–10 |
| Expansion | 6–8 | 11–29 |
| Maturity | 9–13 | 30–49 |
| Late maturity | Over 14 | Above 50 |

Source: Lillis, Narayana and Gilman (1976).

As indicated in Table 1, companies at the penetration stage have operation experience of no more than 5 years. Probably due to constraints in capital, experience and reputation in the market and relative short time in establishing outlets, companies at this stage have a very limited number of outlets. When a company enter the expansion and maturity stage, the number of outlets increases rapidly and reaches its peak at the late maturity stage.

There is a learning curve for foreign investors in host countries (Casseres, 1990). During the early stages of operations, a foreign firm normally requires a local partner. As its experience accumulates, a multi-national company (MNC) will acquire more local knowledge and learning, and develop better organizational capabilities. This in turn leads to a reduced dependency on local partners (Niu, 2001). Some studies confirm that MNCs with more experience in a particular host country tend to expand by means of the full control mode, as befitting their overall strategic position (Agarwal and Ramaswami, 1992). On the basis of the above discussion, it can be concluded that international franchisors from home countries where the franchising system has been well developed prefer complete control on their foreign operations. Therefore, we develop the following hypothesis:

**H3** The more mature a franchising system in the home country, the more likely it is for foreign franchisors to adopt direct international franchising as its entry mode into China.

## 2.4 The Attitude of an International Franchisor toward Risk Spreading

Reasons for a firm to form an alliance with another firm may include resource pooling, asset protection and a greater ability to response quickly to market changes. Facing rapid technological advances, changing market structures and increasing global competition, firms are also motivated to form alliances in order to minimize operational and investment risks (Harriagn, 1988).

Among the most important transitional elements with respect to international investors are risks introduced by the instability and constant reorganisation of economic and political units in emerging marketplaces (Czinkota and Ronkainen,

1997). Such risks are systematically evaluated by Western institutions, including the Economist Intelligence Unit, Institutional Investor, and International Country Risk Guide (ICRG). International franchisors willing to entering into foreign markets ought to learn the framework of government because governmental factors are significant for operations in the host country (Grow, 1986). Market governance influences a wide range of country risk elements such as government regulation and red tape, political stability, bribery, ownership restrictions, controls of capital flows, and import restrictions. These factors are all important to an international franchisor's evaluation of foreign market potential and are essential to determinations of franchise expansion in the international retail arena (Alon and McKee, 1999).

Hence, the following hypothesis is developed:

**H4** The more consideration given by an international franchisor to risk spreading, the less likely it is to adopt direct international franchising as its entry mode into China.

## 3 Research Method

### 3.1 Survey Research Method

Methodologically, international franchising research to date has been largely positivistic and quantitative in nature (Alexander, 1990; Myers, 1995; McIntyre and Huszagh, 1995). Following a positivistic philosophical stance, this research employs a survey using a quantitative research method.

### 3.2 Questionnaire Design

Based on the existing literature and the hypotheses to be tested, a questionnaire with 20 questions was designed, including two open-ended questions to allow participants to provide additional comments. Particular attention has been paid to the wording, form and sequences of the questions.

A pilot study was carried out in August 2005. It involved 20 international franchisors who were familiar with franchising strategic choices from different industry sectors, including firms of restaurant and retailing located in Beijing. Ten copies were sent by e-mail whilst others were sent by post. Two weeks later, 15 copies of the completed questionnaires were returned, giving a return rate of 75%. The results of the pilot study indicated that all of the questions were clear and understandable. However, some participants also provided feedback on the wording of particular questions. Based on the pilot study, some questions were revised.

### 3.3 Sample Origin

A list was compiled from three most important franchising industry sectors—restaurant, retailing, and service. The list included all franchise systems in these industry sectors that were known to have operations in China. During a time span of about four weeks in October 2005, an online survey was sent to a sample frame of 400 firms. The survey was completed by senior managers involved in their firm's strategic decision making. After 3−4 weeks, either phone calls or e-mails were made to those who had not responded. 19 of the 400 questionnaires were returned as undeliverable. Of the 381 questionnaires successfully delivered, 145 questionnaires were returned. Among those 145 responses, 15 invalid responses were excluded from the study bringing the number of useable questionnaires to 130, resulting in an effective response rate of 32.5%. In order to conduct proportion difference analysis, the quantifiable data from these questionnaires was typed and formatted for input into the analysis computer software.

### 3.4 Data Editing and Coding

The data analysis process was managed in three steps: editing and coding the data (including summary statistics of firm characteristics), testing the hypotheses, and conducting a proportion difference test.

Data editing includes getting data ready for coding and transferring to storage, data coding, identifying and classifying each answer with a numerical score or other character symbol. The major findings are summarized in the next section.

## 4 Data Analysis

### 4.1 Summary Statistics of Firm Characteristics

#### 4.1.1 Entry Date

The participants were international franchising firms that have entered into China between 1986 and 2005. The author categorized the market entry dates into four periods: 1980−1989, 1991−1995, 1996−2000, and 2001−2005. Results show that 4% of the respondent entered into China during 1980−1989; 55% during 1991−1995; 27% during 1996−2000 and only 15% during 2001−2005. The data indicates that franchising in China has developed from the introduction stage to expansion stage, and then mature stage.

### 4.1.2 Entry Modes

A majority of international franchising enterprises (63%) selected other entry modes rather than direct international franchising as their entry mode into China. Only 37% selected franchising. This indicates that the majority of participants did not adopt direct international franchising as their choice of entry mode into the Chinese market.

### 4.1.3 Industry Sectors

Sampled firms were divided into three industry sectors: restaurant, retailing, and others. 29% of them were from the restaurant industry, 17% from retailing and 54% from other industries. The data shows that the restaurant industry covers nearly one third of the international franchising firms in China.

### 4.1.4 Home Country of International Franchisors

The sampled firms were divided into four groups according to their home countries: North America, Asia, Europe, and others. The data shows that 53% of international franchising firms come from Asian countries, 31% come from North America, 8% from Europe and other continents. This result supports a conclusion that companies from Asia are motivated to franchise in China as a result of smaller cultural and geographic distance. Accordingly, the majority of international franchising firms in China are from Asia. Therefore, if international franchising firms in North America and Europe can do more to fill the cultural gap, they may obtain more marketing opportunities. This result is consistent with the findings of Fladmoe-Lindquist (1996) and indicates that the less the cultural and geographic distance between host county and home country, the more likely a franchisor to adopt direct international franchising entry mode choice into the Chinese market.

### 4.1.5 Franchise Life Cycle Stage

Based on the life cycle stage as discussed above, stage of franchising systems have been classified into "gradually getting mature" stage and "very mature" stage. Considering the classification proposed by Lillis, Narayana and Gilman in the 1970s, the authors modified outlet numbers for different stages in the questionnaire. The "gradually getting mature" stage refers to firms that have operated in their home market for 9 to 13 years or have 40 to 99 outlets; whilst "very mature" stage refers to firms have operated in their home market over 14 years, or have over 100 outlets.

Our data show that 62% of international franchising firms were at the "gradually getting mature" stage when they entered China, whilst 38% of the firms are at the "very mature" stage. The results suggest that the domestic market saturation is an important factor influencing foreign firms' expansion in China. This result is consistent with the relevant findings made by a number of researchers (e.g., Welch, 1992; Hoffman and Preble, 1993; Hackett, 1976; Hopkins, 1996; Trankheim, 1979; Kedia et al., 1994; Eroglu, 1992).

#### 4.1.6 Number of Outlets

Our survey shows that 34% firms had less than 50 outlets, 23% had 50 to 200 outlets, 24% had 200 to 500 outlets, 10% had 500 to 1 000 outlets, and 9% had more than 1 000 outlets, indicating that the majority of international franchising firms entering Chinese market are small or medium-sized enterprises.

#### 4.1.7 International Market Experience

When the participants were asked how much franchising experience in international markets they have before entering into China, only 7% said that they "have a lot of experience," and 31% declared that they "have some experience" or "very little experience." 62% admitted that they "have no experience" when adopting direct international franchising entry mode choice into China. This result implies that international marketing experience has relatively little impact on an international franchising firm's market entry decision in China.

#### 4.1.8 Risk Spreading Consideration

85% of the participants reported that they "give a lot of attention" to risk spreading when choosing their entry mode into the Chinese market. Only 15% gave no consideration or very little consideration. This result indicates that risk spreading is a significant factor influencing the international franchising firms' entry mode choice when entering into the Chinese market. This finding is consistent with the existing literature (e.g., James and Gary, 2003; Anderson, 1984; Gastrogiovanni, Justis and Julian, 1993).

#### 4.1.9 China's GDP during 1985−2005

China's annual GDP and the number of international franchising firms during 1985–2005 are presented in Fig 1.

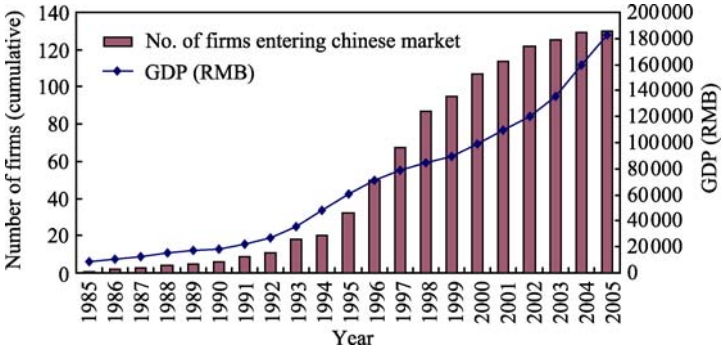


**Fig. 1** GDP versus International Franchisors in China (1985–2005)

Fig. 1 illustrates that the growth in the number of international franchising firms in China is closely related to China's GDP growth. 85% of the participants rated economic growth as either "important" or the "most important" consideration in their evaluation of China as a host country. As the average economic growth rate reached around 9% in China in 1985−2005, more international franchising firms expanded their business in China over this period. The rapid increase in Chinese people's disposable income during the period also helped to create more market opportunities. This result is consistent with the finding that franchisors expand to countries where substantial market opportunities are believed to exist (opportunity recognition) (Fernie and Fernie, 1997). It is also consistent with findings of exploiting potential markets by Hackett (1976), Hoffman and Preble (1993), Welch (1992) and Hopkins (1996); findings of increase sales and profits by Trankheim (1979), Kedia, Ackerman, Bush and Justis (1994) and Hopkins (1996); and findings of perceived favorability of the external environment by Eroglu (1992) and Hoffman and Preble (1993).

## 4.2 Hypotheses Testing: A Proportion Difference Test

In order to investigate the linkage between entry modes and the various characteristics of franchising firms, this research used a proportion difference test. First, the authors defined an entry mode as 1 if the firm chose direct international franchising and 0 otherwise. Second, the sample firms were divided into different groups according to their different characteristics (as per the firm characteristics reported in the previous section). Third, mean comparison tests were used to compare the proportion of firms choosing franchising ($\mu$) across different groups. For example, assuming there are two groups of firms (x and y), which are different in certain characteristics. The proportion of firms choosing franchising

for group x is $\mu_x$ and the one for group y is $\mu_y$. The null hypothesis is $\mu_x = \mu_y$, meaning that there is no significant difference in entry modes between these two groups.

The null hypothesis of $\mu_x = \mu_y$ is tested with the following equation:

$$t = \frac{\overline{x} - \overline{y}}{(s_x^2 / n_x - s_y^2 / n_y)^{1/2}},$$

where $\overline{x}$, $\overline{y}$ are the sample means of the entry mode variable for groups x and y; $s_x^2, s_y^2$ are the standard deviations; $n_x$, $n_y$ are the number of firms. If the $t$ test rejects the null hypothesis at 5% significance level, we deem the difference in entry modes between groups x and y is significant.

### 4.2.1 Relationship between Home Country of Franchising Firms and Entry Modes

Table 2 reports the proportion difference test across franchisors from Asia and the U.S. Results suggest a significant relationship between original country location and franchising entry mode choice. The proportion of Asian firms adopting franchising is significantly higher than the proportion of the U.S. firms. The geographical and cultural distance between China and the other Asian countries is smaller than that of between China and the U.S. We thus conclude that the more similar a franchisor's home country is to China, the more likely it is to adopt direct international franchising as its entry mode into China.

**Table 2** Relationships between Home Country and Entry Mode

| Proportion difference test | $P_{Asian}$ | $P_{North\ America}$ | $P_{Asian} - P_{North\ America}$ |
|---|---|---|---|
| Proportion of firms adopting the direct international franchising entry mode | 38.8 % | 10% | 0.29** (0.16) |

Note: Standard error is reported in parentheses. ** represents significant at 5% level.

This finding is consistent with previous studies showing the importance of distance factors in entry mode choice. For example, Anderson and Gatigon (1986) found that cultural diversity between the franchisor's home country and the host country, particularly regards value and method, can create internal uncertainty as well as problems in business conduct. Hofstede (1980) found that a national culture gap, particularly that between Western and Eastern countries, can sharply affect an organization's management. Taylor, Zhou and Gregory (2000) asserted that East Asian society has different institutional structure from that in North America. Therefore, when East Asian firms enter into overseas

markets, the cultural gap is an important factor influencing their choice of foreign market entry mode.

### 4.2.2 Relationship between Experience and Entry Modes

The current paper divided sample firms into two groups based on their experience in international franchising: those with some experience, and those with little or no experience. The results of proportion difference test are reported in Table 3.

**Table 3** Relationships between International Experience and Entry Modes

| Proportion difference test | $P_{NoExperience}$ | $P_{Experience}$ | $P_{NoExperience} - P_{Experience}$ |
|---|---|---|---|
| Proportion of firms adopting direct international franchising | 36.7 % | 37.5 % | –0.008** (0.09) |

Note: Standard error is reported in parentheses. ** represents significant at 5% level.

The results suggest that there be no significant difference in the proportion of firms choosing franchising between experienced firms and inexperienced firms. This finding does not support H2. However, one limitation of the proportion difference test is that the authors did not control other important influencing factors for entry mode choice. This result is not consistent with the findings of Anderson and Gatignon (1986), Herrman and Datta (2002), and Whitelock (2002), showing that experienced international franchising firms prefer other types of entry modes to the direct international franchising one.

### 4.2.3 Relationship between Firm's Life Cycle and Entry Modes

Similarly, sample firms were divided into immature and mature firms. The results of proportion difference test are reported in Table 4. The percentage of firms choosing franchising in mature firms is significantly higher than that of in the immature group.

**Table 4** Relationships between Maturity and Entry Mode

| Proportion difference test | $P_{Immature}$ | $P_{Mature}$ | $P_{Immature} - P_{Mature}$ |
|---|---|---|---|
| Proportion of firms adopting direct international franchising | 30.0 % | 48.0 % | –0.18** (0.086) |

Note: Standard error is reported in parentheses. ** represents significant at 5% level.

The results suggest that mature firms are more likely to adopt direct franchising mode than other firms. These findings are consistent with extant literature on the linkage between firm life cycle and entry strategy.

### 4.2.4 Relationship between Risk Spreading and Entry Modes

Sample firms were divided into another two groups based on their attitude towards business risk in franchising, as shown in Table 5.

**Table 5** Relationships between Risk and Entry Modes

| Proportion difference test | $Pa_{Norisk}$ | $P_{Risk}$ | $P_{Norisk} - P_{Risk}$ |
|---|---|---|---|
| Proportion of firms adopting direct international franchising | 25.0 % | 42.2 % | –17.2 %** (0.091) |

Note: Standard error is reported in parentheses. ** represents significant at 5% level.

Our result shows that risk-averse firms are less likely to adopt direct international franchising entry mode. This finding is consistent with previous findings that risk consideration is an important explanation for direct international franchising strategy (James and Gary, 2003; Harriagn, 1988).

## 4.3 Hypotheses Testing: Regression Analysis

Logistic regression analysis is widely used as a method to predict the occurrence of a dependent variable (Anderson and Coughlan, 1987; Klein and Roth, 1990; Ramaseshan and Patton, 1994). In order to further examine the influence of particular factors on the entry mode choice of international franchising firms, this study adopted the logit model as a key statistical analysis tool. Specifically, the authors used the following equation:

$$\Pr(Y_i = 1) = F(X_i\beta) = \frac{\exp(X_i\beta)}{1+\exp(X_i\beta)}, \quad (1)$$

where $Y_i$ is a dummy variable, which equals to 1 if firm $i$ chooses direct international franchising or 0 if the firm chooses other entry modes. $X_i$ measures various characteristics of firm $i$, including the following variables:

(1) Industry dummy $I_{ij}$ which is equal to 1 if firm $i$ operates in industry $j$, or 0 otherwise.

(2) Entry date dummy variables, $D1990$ and $D2000$, which measure the entry date of firms into China. $D1990$ equals 1 if a firm entered the Chinese market during the 1990s and 0 otherwise. $D2000$ equals 1 if a firm has entered the Chinese market during the 2000s and 0 otherwise. The benchmark is the firms entered into China during the 1980s.

(3) Two home country dummy variables, *DNorth America* and *DEurope*, which represent the home country of the international franchising firms. *DNorth America* equals 1 if a firm comes from North America and 0 otherwise. Likewise, *DEurope* equals 1 if the firm comes from Europe and 0 otherwise. The

benchmark is Asian firms.

(4) Maturity dummy, *DMaturity*, which equals 1 if a firm is very mature, and 0 if a firm is immature.

(5) Risk consideration dummy, *DRisk*, which equals 1 if a firm considers minimizing its operating risk when choosing its entry strategy, and 0 otherwise.

(6) Experience dummy, *DExperience*, which equals 1 for no experience, and 0 otherwise.

The log-likelihood equation adopted in this article is as follows:

$$\ln L = \sum_{Y_i=1} \ln F(X_i\beta) + \sum_{Y_i=0} \ln[1 - F(X_i\beta)]. \quad (2)$$

The maximum likelihood estimation is used to estimate the coefficient $\beta$. The estimated coefficients $\hat{\beta}$ from the logit model are reported in the following table:

**Table 6** Determinants of Entry Mode Choices of International Franchising Firms

| | Logit Model |
|---|---|
| *D*1990 | 0.555 |
| | (0.74) |
| *D*2000 | 0.180 |
| | (0.22) |
| *DNorth America* | –2.972** |
| | (–2.10) |
| *DEurope* | –4.823** |
| | (–2.37) |
| *DMaturity* | 2.028** |
| | (2.33) |
| *DRisk* | 2.196* |
| | (1.81) |
| *DExperience* | –2.064** |
| | (–2.01) |
| Constant | –0.213 |
| | (–0.19) |
| Industry dummies | Yes |
| *R*-square | 0.11 |
| Observations | 130 |

Note: *Z*-values are reported in the parentheses. * and ** represent 10% and 5% significance level, respectively.

## 4.4 Comparison of Our Conclusions with Earlier Studies

The results from the logit model are reported in Table 6. As shown, the time dummies (*D*1990 and *D*2000) are statistically insignificant. This means that entry period has no significant impact on entry mode choice. The home country dummies (*DNorth America* and *DEurope*) are negative and statistically

significant. This suggests that Asian firms are more likely to choose direct international franchising than firms from North America or Europe. Since Asian countries are closer to China in both cultural and geographical distance, this result supports H1: The greater the cultural and geographical distance between China and the home country, the less likely the international franchisor is to adopt direct international franchising. This finding is consistent with the previous studies conducted in developed countries which indicated cultural distance plays an important role in entry mode choice. Anderson and Gatigon (1986) found that cultural distance between a franchisor's home and host country can create internal uncertainty as well as problems in business conduct. Hofstede (1980) found that national cultural gap, particularly a Western and Eastern cultural difference, sharply affects an organization's management. Taylor, Zhou and Gregory (2000) found that the East Asian society has different institutional structure than that in Western nations. Therefore, when East Asian firms enter into overseas markets, cultural gap is a key factor influencing foreign market entry decisions.

The estimated coefficient of the Experience dummy *DExperience* is negative and significant at the 5% significance level. This supports H2 that foreign market experience has a significant impact on the international franchising firm's market entry strategy. This finding is consistent with previous studies which found that international experience significantly affected the firm's entry mode.

Table 6 shows that the estimated coefficient of the dummy variable of Maturity is 2.028 (statistically significant from 0). This implies that mature firms are more likely to choose direct international franchising than growing firms. The Maturity dummy measures the stage in the life cycle of international franchising firms. These results support H3 that mature firms are more likely to adopt direct international franchising. These findings are consistent with the literature on the linkage between firm life cycle and entry mode choice.

Table 6 shows that the estimated coefficient for the dummy variable of Risk is positive and significant at a 10% significance level. It suggests that risk consideration does have a strong effect on entry mode choice. This result supports H4 that franchising firms that consider minimizing their operating risk are less likely to choose direct international franchising as their choice of entry mode.

## 5 Conclusion

The main objective of this study is to examine key factors and their impact on the international franchisors' entry mode choices in China. After collecting and analyzing the survey data, this research finds that international franchising systems from Asia are more likely to choose direct international franchising entry

mode into China than the firms from North America and Europe do. This indicates that the less the cultural and geographical distance between home country and host country, the more likely the international franchisor is to adopt franchising. Firm maturity also has an important effect: Firms at an expansion stage are more likely to choose franchising than firms in an introduction stage. Mature firms are more likely to choose direct international franchising than the immature firms. Moreover, risk spreading is a key consideration influencing whether international franchising firms adopt direct international franchising or other choice of entry mode. However, being different from the existing literature in which it is claimed that international experience is an important factor for the international franchisors to consider when entering countries like the U.S., Russia and India, this research indicates that this factor does not have a significant effect on franchising entry mode choice into the Chinese market.

Although the main findings of this study are consistent with the extant literature which is mainly derived from developed countries, contributively, this study offers new insights that extend mainstream foreign investment theory and provides a different way to understand the entry strategies in the context of international franchisors entering into developing countries. From the theoretical perspective, this study supplements the extant literature by investigating important factors which influence the international franchisors' entry modes into China. In addition to the theoretical contribution, this study also has significant managerial implications to guide both policy makers and managers to consider the international entry mode choices. Other studies could use our findings as a basis to extend research in this area.

Although this research has considerable contributions to both extant literature and practical exercise, it is not free from limitations. The survey was carried out in first-tier and second-tier Chinese cities where most international franchising firms located when they first entered into the Chinese market. It may not represent the strategy for firms in remote areas and small cities in China due to different economic environments and sub-business cultures in different locations. Furthermore, this research does not look into the performance of these international franchisors, but rather focuses on the relationship between factors and the entry mode choices. Future research can be carried out by examining relationship between performances of firms and different entry mode choices to have a better understanding of how international franchising managers make entry mode decisions in China.

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