UNIT–4: ENTERPRISE GROWTH STRATEGIES

"Entrepreneurship is living a few years of your life like most people won't so you can spend the rest of your life like most people can't."

– Warren G. Tracy's student

Learning Objectives:

The learner would be able to:

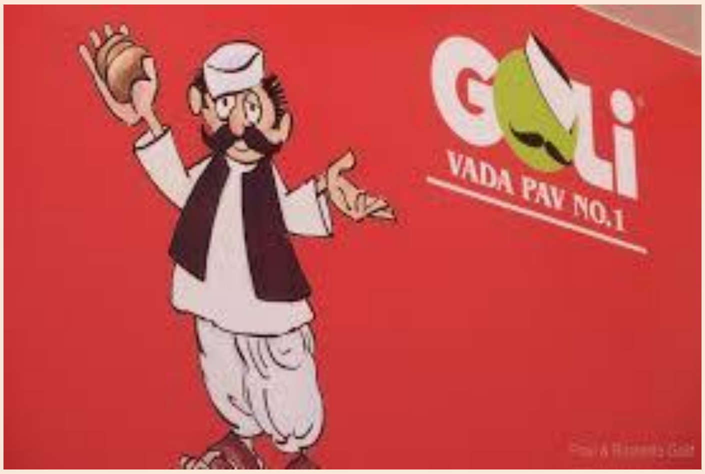
- Explain in detail about franchising
- Understand the types of franchising
- Understand how growth of a firm is possible through mergers and acquisitions
- Enlist the types of mergers
- Elaborate on the meaning and types of acquisitions
- Understand the reasons for mergers and acquisitions
- Understand the reasons for failure of mergers and acquisitions
- Explain the concept of value addition
- Understand the meaning of value chain
- Understand the requirements for value chain management

Content

- **Franchising**
- **Mergers and Acquisitions**
- **Value Addition and moving up the Value Chain**

Case Study-I
Goli Vada Pav

Launched in 2004, Goli Vada Pav repackaged 'Vada Pav', a humble street-food popular in Mumbai, into a branded fast food concept. It follows franchise business model and today is uniquely positioned in Indian QSR (quick service restaurant) segment. Read on to discover more about the brand's success and growth journey.



Origin and Concept

Goli Vada Pav, a quick serve food concept with authentic Indian touch, originated in Mumbai in 2004. The brand's founders, Venkatesh Iyer and Shiv Menon, realised the huge scope of business in tapping the adult and lower income customers by selling widely popular local street food 'Vada Pav' to them, in an organised way. Thus, the idea of Indian finger food Goli Vada Pav Pvt Ltd was born that retailed the humble mouth watering spicy ethnic delicacy, which was pocket friendly as well as prepared and served in hygienic conditions. Indian QSR market is flooded with brands like McDonald's, Subway and Quiznos but the success of Brand – Goli Vada Pav No. 1 reaffirms the fact that a strong home grown concept can not only thrive but also compete with International Brands.

What makes concept so special?

Vada Pav is basically a spicy vegetable patty in bun sold by street-food vendors. The brand Goli Vada Pav No. 1 has pioneered the concept of selling vada pav through retail outlet. The brand's stores offer quality and hygienic fast food which is quite affordable. It has successfully branded the traditional street food. It sells hygienically prepared food items made in fully automated 'HACCP' certified handsfree plant with an authentic touch. 'Goli Vada Pav' is a typical finger food made of spices, vegetables, and mashed potatoes packed in 'vada pav'. Today, it is known to be an established, reputed, and popular Indian fast-food brand that offers a clean and ethnic finger food for those who have less money and time.

Popular products

The brand offers wide assortment of items to cater to varied taste buds and preferences of customers. Its outlets serve different finger dishes like sweet chutney, dry chutney, and fried green chilly. Its famous dishes include Goli Schezwan Vada Pav, Goli Cheese Vada Pav, Goli Sabudana Vada, Goli Mix Veg. Vada Pav, Goli Tikki Vada Pav, Goli Palak Makkai Tikki, Goli Cheese Ungli, and Goli Masala Vada Pav. As the name suggests vada is a common thing, which is mixed with other thing for different taste. The company's food offerings not only entice the taste buds of consumers, but they are also touted to be nutritional.

Success journey till now

The brand has opted for franchise business models to grab a quick bite into the Indian quick serve business. Today, Goli Vada Pav has extensive presence across 40 Indian cities in six states. Goli Vada Pav No. 1 outlets are spread across the length and breadth of the country. Its stores can be found in cities like Aurangabad, Ahmednagar, Bangaluru, Belgaum, Chandrapur, Chennai, Coimbatore, Dhulia, Hubli, Hyderabad, Jalgaon, Kolhapur, Mumbai, Pune and many more. It operates about 150 stores, of which over 140 are via franchise route.

Lucrative business opportunity

The brand's concept offers lucrative business opportunity for aspiring franchisees. The factors that make this concept a money spinner are:

Vada Pavs are popular all-time favourite and convenient fast food. The product is hygienic and less oil fried snack having universal appeal. It's a standard tasty food that can be consumed 365 days of the year. The store format and operations are relatively less cumbersome. The product is easy to make and it being a finger food one doesn't require plates, spoons, tables and chairs to eat it. It is a mobile food that can be consumed while walking, talking, standing or travelling, and is therefore preferred by people on the move. Therefore, the franchisee store owner would not require huge investments like infrastructure, kitchen and restaurant etc which substantially cut the input costs.

Franchising facts

The company is looking to strengthen its pan India franchisee network. It is targetting especially tier I, tier II, tier III cities and small towns for expansion and opening more number of stores. It would like to partner with potential franchise partners who can invest ₹ 10-20 lakh. For opening a Goli Vada Pav No. 1 store, area requirement is about 350 sq ft. The preferred location for opening an outlet is a high street traffic areas like market, colleges, business areas and residential catchments.

Franchisee training and support

The franchisee will get the eight-year old well established brand name with standard operating procedures in all aspects of business. The company will provide initial and refresher training for business owners and store staff and end-to-end logistics support & regular replenishment of stocks and operational support to monitor and drive business.

Franchising adds flavour to further growth

The brand's offerings are economical and for the masses, therefore it has access to a large customer base. It is committed to take vada pav from the Mumbai streets to a brand which will be known all over the world. Growing popularity of the concept has encouraged Goli Vada Pav No. 1 to continue with its expansion plans. The brand encourages entrepreneurship and offers lucrative franchise opportunities across India. The company plans to have 500 outlets by the end of the year 2015.

Courtesy: Franchiseindia.com

A. Growth and development of an enterprise

Growth is always essential for the existence of a business concern. A concern is bound to die if it does not try to expand its activities. The entrepreneur is an endless challenge seeker. Once their small business is humming along, growth is the next exciting challenge. The decision to extend the scope of one's business must be a result of thoughtful consideration of various factors, including the financial, logistical, even his/her emotional readiness. The rule of thumb is that one should only expand when there are untapped opportunities that can benefit the business. There may be a niche that

you want to capture or a location not serviced even by your competitors. Expansion is often one of the most daunting challenges a successful business will face.

Ron Sommer, former president, Sony Corporation of India: says "Where a company comes from is less important than where it is going, as boundaries are erased, corporate birth certificate won't count much." The successful entrepreneur will make sure there is a constant flow of new ideas and a commitment to try out at least some of these new ideas. An organization has to maintain its momentum through interplay of flexibility and change. This calls for growth and development which in essence is achieved through constant strife.

An entrepreneur has a dual role to play- one, that of a leader and the other of a manager. The former provides direction and energy while the latter processes the input and gives the output. To ensure the continued efficiency and profitable functioning and growth of enterprise, extra managerial ability is required.

The expansion of a concern may be in the activities or acquisition of ownership and control of other concerns. Thus, expansion may be;

- Internal Expansion
- External Expansion

i) Internal expansion

Internal expansion results from the gradual increase in the activities of the concern. The concern may expand its present production capacity by adding more machines or by replacing old machines with the new machines with higher productive capacity. The internal expansion can also be undertaken by taking up the production of more units or by entering new fields on the production and marketing sides. Internal expansion may be financed by the issue of more share capital, generating funds from old profits or by issuing long-term securities. The net result of internal expansion is the increase in business activities and broadening the present capital structure.

ii) External expansion or business combination

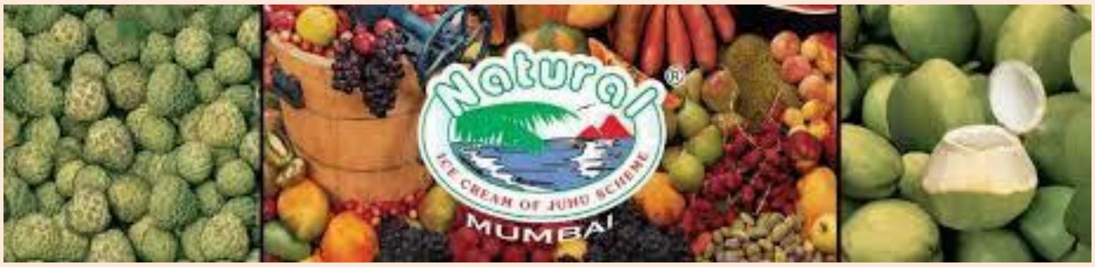
External expansion refers to business combination where two or more concerns combine and expand their business activities. In the process of combination, two or more units engage in similar business or related process or stages. Sometimes stages of the same business join with a view to carry on their activities or shape, their polices on common basis some other or in coordination for mutual benefit or maximum profits. The combination may be among competing units or units engaged in different processes. After combination, the constituted firm pursues some common objectives or goals.

In this unit, we will focus on the main forms of external expansion which are

a) Franchising

b) Mergers and Acquisitions

Case Study-II
It's natural. It's yummy: It's NATURAL ICE CREAM



It's natural. It's yummy. Those who have tasted it, swear by it. The unique feature of the ice creams manufactured by Natural Ice Cream is that they contain no artificial flavours, preservatives or stabilisers, only fresh fruit pulp or dry fruits.

Started as a 300-sq-ft ice cream parlour at Juhu, a northwest Mumbai suburb, in 1984, the brand is a runaway success. It now has 89 franchise outlets across West and South India: 47 in Mumbai, 29 in the neighbouring urban clusters of Navi Mumbai, Thane and Pune, and the rest scattered across selected cities of Maharashtra and neighbouring states. Ten more will be opened in the current financial year. Natural's revenues have grown from ₹14 lakh in 1986 to ₹40 crore in 2010-11. The franchises may be many, but the manufacturing hub is just one, located in another Mumbai suburb, Kandivali. Every morning, a fleet of trucks rolls out from the factory carrying the ice cream to all the Natural outlets, thus ensuring quality is not compromised.

The store at Juhu has been renovated and expanded repeatedly, and is now more than three times its original size. "It is a landmark in the area," says a beaming Kamath. It all began after Kamath broke away from his elder brother's ice cream business, Gokul Ice Cream, in 1983. "I took my share of the inheritance and set up Natural," says Kamath. From the start he was at enormous pains to keep to quality - a trait he maintains to this day. Seasonal fruits are bought in bulk daily from the market, with only the best quality ones being chosen. The extracted pulp is heated, to get rid of unwanted bacteria, and then stored in aluminium-sealed packages.

Kamath, who from the start involved himself in every aspect of manufacture and distribution, says he has experimented with 60 different kinds of fruit. (In case of non-seasonal fruits, however, Kamath has no choice but to buy pulp and get it machine processed.)

The means Natural uses to enforce quality control, however, impose their own limits on the brand's expansion. All the temperature control in the world cannot preserve the taste - and more importantly the freshness - of ice cream beyond a specified number of hours, during which Natural's trucks can cover only a finite distance. This explains why Natural's outlets are largely in Western India, and it has no outlet yet in the national capital, despite the obvious business opportunity Delhi presents. "The National Capital Region has remained an elusive destination," admits Pai.

But the scenario may soon change. Though Natural officials are reluctant to share details of their financial relationship with the franchises, they do reveal that plans are afoot for a major change in operational strategy. The man responsible is Kamath's son, Srinivas, who was inducted into the business in 2009. Srinivas, 27, believes that since it is dealing in perishable products such as ice cream, Natural has to set up manufacturing units in other locations, if it wants to keep expanding.

Srinivas wants to set up 'mega shops' in faraway cities and towns, which will both manufacture Natural ice cream and sell it. "Raw material will be supplied from here, as well as trained workers who will make the ice cream at the mega shops," says Srinivas. "Frozen, non-perishable fruit pulp and processed milk can be stored for a maximum of four days without harm. That is enough time to transport them to wherever the mega shops are opened."

Again, in a change of strategy, Natural intends to open only one shop in these faraway areas. "Instead of investing in multiple franchises, Natural will have just one mega shop per town," Srinivas adds. Natural will also impose its conditions: the outlet must have at least 2,000 square feet floor space and must be located in a central area. The first such outlet is set to open shortly in Chandigarh; depending on its success, more such shops will follow.

Natural is in no hurry to get to Delhi, but it has big plans when it does. "Delhi is a very big market. To meet its demand, we'll have to double our existing capacity," says Pai. Natural's ambitions go even further. "Our founder wants Delhi to be the launch pad for Natural's global ventures, especially in West Asia," he adds.

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Franchising

Franchising began back in the 1850's when Isaac Singer invented the sewing machine. In order to distribute his machines outside of his geographical area, and also provide training to customers, Singer began selling licenses to entrepreneurs in different parts of the country. In 1955 Ray Kroc took over a small chain of food franchises and built it into today's most successful fast food franchise in the world, now known as McDonald's. McDonald's currently has the most franchise units worldwide of any franchise system.

Today, franchising is helping thousands of individuals be their own boss and own and operate their own business. Franchising allows entrepreneurs to be in business for themselves, but not by themselves. There is usually a much higher likelihood of success when an individual opens a franchise as opposed to a mom and pop business, since a proven business formula is in place. The products, services, and business operations have already been established.

Franchising opportunities have often evolved from changes in the environment as well as important social trends.

Franchising is as "an arrangement whereby the manufacturer or sole distributor of a trademarked product or service gives exclusive rights of local distribution to independent retailers in return for their payment of royalties and conformance to standardized operating procedures". The person offering the franchise is known as the *franchisor.* The *franchisee* is the person who purchases the franchise and is given the opportunity to enter a new business with a better chance to success than if he or she were to start a new business from scratch. Foundation of this relationship is the Franchise Agreement.

A *franchise agreement* is the legal document that binds the franchisor and franchisee together. This document explains what the franchisor expects from the franchisee in running the business. The agreement is designed to assure that all of the franchisees within an organization are treated equitably. The expectations must be uniform throughout the system.

The main ingredients of a franchise agreement:

- **Contract Explanation:** The contract explanation is the part of the agreement that outlines the type of relationship a franchisee is entering into with the franchisor.
- **Operations Manual:** The operations manual is the section of the agreement that details the guidelines that the franchisee must legally follow in operating the business as outlined by the franchisor. From time to time amendments may be made and the franchisee must be prepared to adjust operations accordingly. The franchisee needs to be aware that the contents of the document are confidential.
- **Proprietary Statements:** Proprietary statements outline how the franchise name is to be used, as well as the marketing and advertising procedures in place that the franchisee will be required to follow. Also, the franchisor documents how much the franchisee will be required to contribute toward national advertising efforts.
- **Ongoing Site Maintenance:** Ongoing site maintenance is another item that is outlined in the agreement. Included are the types and timeframes regarding various maintenance items and upgrades that must be made to the franchisee's location.

As in any legal document, it is recommended that you have your attorney review the franchise agreement before signing.

Big brands make head towards for franchising

The big corporate houses that have opted for a franchise route consider franchising as an easy mode of expansion with commitment level of the franchisor and the franchisees. It is a powerful and ideal way to expand business, for a company which does not have any capital, manpower or time to build the network of company-owned outlets.

However, Dabur is not the first big established brand that has taken up franchising for expansion. There are various other corporate houses that have been into franchising for quite some time now and have marked their presence not just pan-India, but also global.

Raymond Ltd, a company started in 1925 as a woollen and readymade garment industry, has achieved phenomenal success with more than 500 stores. As Anirudh Deshmukh, President, Raymond Ltd, says, 'Raymond can be called the "absolute leaders" in the fabric industry as consumers had faith on us for the last 50 years and still we are growing stronger. We basically opted for franchise model for expanding in smaller towns as these are not affected by recession and the franchised stores can be driven by local entrepreneurs who are aware of the preferences of the local customers.

NIIT, a well-known name in the IT education industry, has a franchising network of more than 12,500 centres spread over in more than 40 countries worldwide, apart from India. As per G. Raghavan, President, Global Learning Solutions, NIIT, 'A large part of this success has been possible due to our business partners, who have been a crucial element of our fabric. The Business Partner Network not only helped NIIT expand its presence across India and reach the unreached, it also fuelled the fire of entrepreneurship in the country.

JSW Steel Ltd., the third-largest Steel manufacturer in India, operates through 174 JSW Shoppe outlets that work on the franchise model. Now, the company is planning to take the count of its JSW Shoppe outlets to 340 by 2011.

Mahindra & Mahindra Ltd. a part of the India industrial conglomerate Mahindra Group, has taken the franchise route to expand its 100 per cent subsidiary, Mahindra First Choice, a multi-brand car-servicing company. The company is planning to take the count of its outlets to 450 in the next four years. The new outlets will be a mix of both company-owned and franchise outlets. Can also refer to the Case study of Satya Barta Dey – SHREE LEATHERS Unit 2, sub–heading **Growing, growing, franchising,** to understand aptly what is meant by' if you do not grow, you cannot endure'.

Types of franchising

Before you dive head first into your franchise business opportunity search, it's important that you understand the four different types of franchising opportunities available to you.

Product franchise business opportunity: Manufacturers use the product franchise to govern how a retailer distributes their products. The manufacturer grants a store owner the authority to distribute goods by the manufacturer and allows the owner to use the name and trademark owned by the manufacturer. The store owner must pay a fee or purchase a minimum inventory of stock in return for these rights. Some tire stores are good examples of this type of franchise.

Manufacturing franchise opportunity: These types of franchises provide an organization with the right to manufacture a product and sell it to the public, using the franchisor's name and trademark. This type of franchise is found most often in the food and beverage industry. Most bottlers of soft drinks receive a franchise from a company and must use its ingredients to produce, bottle and distribute the soft drinks.

Business franchise opportunity ventures: These ventures typically require that a business owner purchases and distributes the products for one specific company. The company must provide customers or accounts to the business owner, and in return, the business owner pays a fee or other consideration as compensation. Examples include vending machine routes and distributorships.

Business format franchise opportunity: This is the most popular form of franchising. In this approach, a company provides a business owner with a proven method for operating a business using the name and trademark of the company. The company usually provides a significant amount of assistance to the business owner in starting and managing the company. The business owner pays a fee or royalty in return. Typically, a company also requires the owner to purchase supplies from the company.

How Franchising help start-ups:

1. Franchising changed the working of the startups because already the product carriers a name in the market already which is the most difficult part of business to establish. That is why the startups pay royalty to the franchisor. Since the startups offer an established product that struggling time and money involved in the process. Startups save that.
2. Startups take up training to understand the product and franchisors make franchises fully conversant with the product/services that they have to offer. It is very important that the Sales-man must know his/her product. In this case, start-ups are the sales person. And franchisors charge a fee for this purpose, franchisors motive is at every step 'Pay and Smile. That is not a bad bargain.
3. The start-ups can grow fast without having to increase labour, operating costs and blocking running expenses because normally buyers straight walk up to them.
4. In practical Franchises work for the benefit of franchisors in other words they turn up one plus one eleven. Both are all out open to help each other. Franchisors' efforts to boast their franchises are always sincere, so there is no–clash of interest.

Advantages of franchising

One of the most important advantages of buying a franchise is that the entrepreneur does not have to incur all the risks associated with creating a new business. Typically, the areas that entrepreneurs have problems with in starting a new venture are product acceptance, management expertise, meeting capital requirements, knowledge of the market, and operating and structural controls. In franchising, the risks associated with each are minimized through the franchise relationship, as discussed below.

Advantages to the franchisee

1. Product acceptance

The franchisee usually enters into a business that has an accepted name, product or service. In the case of Subway, any person buying a franchise will be using the Subway name, which is well known and established throughout the United States. The franchisee does not have to spend resources trying to establish the credibility of the business. That credibility already exists based on the years the franchise has existed. Subway has also spent millions of dollars in advertising, thus building a favourable image of the products and services offered. An entrepreneur who tries to start a sandwich shop would be unknown to the potential customers and would require significant effort and resources to build credibility and a reputation in the market.

2. Management expertise

Another important advantage to the franchisee is the managerial assistance provided by the franchisor. Each new franchisee is often required to take a training program on all aspects of operating the franchise. This training could include classes in accounting, personnel management marketing and production. McDonald's, for example, requires all its franchisees to spend time at its school, where everyone takes classes in these areas. In addition, some franchisors require their new franchisees to actually work with an existing franchise owner or at a company-owned store or facility to get on-the job training. Once the franchise has been started, most franchisors will offer managerial assistance on the basis of need. Toll-free numbers are also available so that the franchisee can ask questions anytime. Local offices for the larger franchises continually visit the local franchisees to offer advice and keep the owners informed of new development.

The training and education offered is actually an important criterion that the entrepreneur should consider in evaluating any franchise opportunity. If the assistance in start-up is not good, the entrepreneur should probably look elsewhere for opportunities unless he or she already has extensive experience in the field.

3. Capital requirements

As we've seen in previous chapters, starting a new venture can be costly in terms of both time and money. The franchise offers an opportunity to start a new venture with up-front support that could save the entrepreneur's significant time and possibly capital. Some franchisors conduct location analysis and market research of the area that might include an assessment of traffic, demographics, business condition and competition. In some cases, the franchisor also finances the initial investment to start the franchise operation. The initial capital required to purchase a franchise generally reflects a fee for the franchise, construction costs and the purchase of equipment.

The layout of the facility, control of stock and inventory and the potential buying power of the entire franchise operation can save the entrepreneur significant funds. The size of the parent company can be advantageous in the purchase of health care and business insurance, since the entrepreneur would be considered a participant in the entire franchise organization. Savings in start-up are also reflected in the pooling of money by individual franchisees for advertising and sales promotion. The contribution by each franchisee is usually the function of the volume and the number of franchises owned. This allows advertising on both local as well as national scale to enhance the image and credibility of the business, something that would be impossible for a single operation.

4. Knowledge of the market

Any established franchise business offers the entrepreneur years of experience in the business and knowledge of the market. This knowledge is usually reflected in a plan offered to the franchisee that details the profile of the target customer and the strategies that should be implemented once the operation has begun. This is particularly important because of regional and local differences in markets. Competition, media effectiveness, and tastes can vary widely from one market to another. Given their experience, franchisors can provide advice and assistance in accommodating any of these differences.

Most franchisors constantly evaluate market conditions and determine the most effective strategies to communicate to the franchisees. Newsletters and other publications that reflect new ideas and developments in the overall market are continually sent to franchisees.

5. Operating and structural controls

Two problems that many entrepreneurs have in starting a new venture are maintaining quality control of products and services and establishing effective managerial controls. The franchisor, particularly in the food business, identifies purveyors and suppliers that meet the quality standards established. In some instances, the supplies are actually provided by the franchisor. Standardization in the supplies, products and services provided helps ensure that the entrepreneur will maintain quality standards that are so important. Standardization also supports a consistent image on which the franchise business depends for expansion.

Administrative controls unusually involve financial decisions related to costs, inventory and cash flow and personnel issues such as criteria for hiring/firing, scheduling and training to ensure consistent service to the customer. These controls are usually outlined in manual supplied to the franchisee upon completion of the franchise deal.

Although all the above are advantages to the franchisee, they also represent important strategic considerations for an entrepreneur who is considering growing the business by selling franchises. Since there are so many franchise options available for an entrepreneur, the franchisor will need to offer all of the above services in order to succeed in the sale of franchises. One of the reasons for the success of such franchises as McDonald's, Burger King, KFC, Boston Market, Subway, Midas, Jiffy Lube, Holiday Inn, Mail Boxes and Merry Maids is that, all these firms have established an excellent franchise system that effectively provides the necessary services to the franchisee.

Advantages of franchising to the franchisor

The advantages a franchisor gains through franchising are related to expansion risk, capital requirements and cost advantages that result from extensive buying power. It is clear from the Subway example that Fred DeLuca would not have been able to achieve the size and scope of his business without franchising it. In order to use franchising as an expansion method, the franchisor must have established value and credibility that someone else is willing to buy.

Quick expansion

The most obvious advantage of franchising for an entrepreneur is that it allows the venture to expand quickly using little capital. This advantage is significant when we reflect on the problems and issues that an entrepreneur faces in trying to manage and grow a new venture. A franchisor can expand a business nationally and even internationally by authorizing and selling franchises in selected locations. The capital necessary for this expansion is much less than it would be without franchising. Just think of the capital needed by DeLuca to build 8,300 Subway sandwich shops!

The value of the franchise depends on the track record of the franchisor and on the services offered to the entrepreneur or franchisee. Subway's low franchise fee has enhanced expansion opportunities, as more people can afford it.

Operating a franchised business requires fewer employees than a non-franchised business. Headquarters and regional offices can be lightly staffed, primary to support the needs of the franchisees. This allows the franchisor to maintain low payroll and minimizes personnel issues and problems.

Cost advantages

The mere size of a franchised company offers many advantages to the franchisees. The franchisor can purchase supplies in large quantities, thus achieving economies of scale that would not have been possible otherwise. Many franchise businesses produce parts, accessories, packaging and raw materials in large quantities, then in turn sell these to the franchisees. The franchisee are usually required to purchase these items as part of the franchise agreement and they usually benefit from lower prices.

One of the biggest cost advantages of franchising a business is the ability to commit larger sums of money to advertising. Each franchisee contributes a percentage of sales (1 to 2 %) to an advertising pool. This pooling of resources allows the franchisor to conduct advertising in major media across a wide geographic area. If the business had not been franchised, the company would have to provide funds for the entire advertising budget.

Disadvantages of franchising to the franchisee

Since there are multiple advantages of growing a business through the franchise mode, certain disadvantages also exist that need to be carefully examined. The greatest problem mainly arises as an outcome of differences between the franchisor and franchisee in terms of certain formal and informal commitments that do not get operationalized. Some of the key disadvantages of this mode of expansion are:

- **Right and the only way of doing things:** Entering into a franchise contract limits the degree of freedom for the franchise. As such, one gets an over-guided and over-influenced degree of control exerted by the franchisor. This results in losing the freedom to innovate to some extent.
- **Continuing cost implication:** Over and above the original franchise fee and royalties, a percentage of revenue gets shared perpetually with the franchisor. The franchisor may also charge additional amounts towards sharing the cost for services provided such as advertising and training. As such, entering into franchise contracts with a well-known franchisor becomes a very expensive proposition because of a tendency on their part to exploit the franchisee.

- **Risk of franchisor getting bought:** The franchisee faces serious problems and difficulties when the franchisor either fails or gets bought out by another company.

No one knows this better than Vicent Niagra, an owner of three Window Works franchises. Niagra had invested about $1 million in these franchises, when the franchise was sold in 1988 to Apogee Enterprises and then resold in 1992 to a group of investors. This caused many franchises to fail, leaving a total of 50. The failure of these franchises has made it difficult for Niagra to continue because customers are apprehensive about doing business with him for fear that he will go out of business. No support services that had been promised were available.

- **Inability to provide services:** The disadvantages to the franchisee usually centre around the inability of the franchisor to provide services advertising and location. When promises made in the franchise agreement are not kept, the franchisee may be left without any support in important areas. For example, Curtis Bean bought a dozen franchises in Checkers of America Inc., a firm that provides auto inspection services. After losing $200,000, Bean and other franchisees filed a lawsuit claiming that the franchisor had misrepresented advertising costs and had made false claims including that no experience was necessary to own a franchise.

Disadvantage to the franchisor

Difficulty in identifying quality franchisees: Above all, even the franchisor may find it difficult to identify quality franchisees. Even after extending all support towards training and providing capital, poor management may lead to the failure of the franchisee and in turn, adversely affect the franchise system as a whole.

Case Study-III
Indian franchise boom

For small and first time entrepreneurs in India, taking up franchise of a well-established brand is a good proposition. Buying a franchise of an established brand is a good alternative to starting on a new idea from scratch or could offer a faster way to take an existing business to the next level. To list a few;

Gift a flower… ….and a cake….and a candle….

Ferns N Petals, founded by Vikaas Gutgutia, a Delhi based company, and the leading brand of floral boutiques in India is marked as a one-stop-shop for all flower requirements, whether it is for daily or occasional gifting, for floral decoration in weddings, corporate events or for an individual parties. Floral boutiques are aesthetically designed and its air – conditioned outlets reflect style and high taste to cater to elite customers. FNP's floral boutique offers a vast variety of fresh cut flowers and unique flower arrangements, artificial & dry flowers, and an exclusive range of object d'art such as scented candles, candle stands, imported Italian glass vases, wooden gift accessories with intricate carving, photo-frames, miniature exportable gift items, fragrance items based on aromatherapy and potpourris, etc. These boutiques offer a vast variety of exquisite flower arrangements and displays to match the distinct needs and tastes of the customers. Growth of FNP, too, is attributable to franchising.

Food Courts work well with franchising models

Haldiram Franchise – A Profitable Business Opportunity

The food and beverage industry has not experienced any crunch, mainly because the people are spending money in a big way on eating out, together with entertainment. The Indian economy is growing rapidly, automatically creating more room for the growth of this industry.

The Haldiram Marketing franchise is associated with sweets and namkeens for the discerning consumers for the past six decades in India and across the world. The food and beverage franchise made a modest start in the beginning of 1941 in Bikaner in the State of Rajasthan in India. According to the sweet and savory products franchise, sweet and salt are opposite to each other, but they perform wonders on the taste buds.

The Haldiram Marketing franchise uses both sweet and salt in its foods, with mithais (sweets) and namkeens (salty snacks). This unique concept of the food and beverage franchise has made it to be a leader in the sweet industry and it has also maintained this position for many years. The sweet and savoury products franchise has been synonymous with sweets similar as Cadbury is to Chocolates.

The Haldiram Marketing franchise can by default be termed as taste of tradition of India. The sweet and savoury products franchise has certain prospective markets, such as those in China, Russia, the United Kingdom, Madagascar and Ukraine, for promoting and marketing the brand of Haldirams.

Among various food joints from domestic sector, Haldiram franchise has carved a separate niche for themselves. Haldiram made a humble beginning, when it commenced its business in Bikaner, in the state of Rajasthan. Since then, the food and beverage franchise has witnessed phenomenal growth and is currently a renowned manufacturer of sweets across the globe. The sweet and savory products franchise has a chain of restaurants and is also anticipated to start amusement parks.

The Haldiram franchise is the flag bearer of the traditional Indian sweet. This food and beverage franchise was started by Shri Ganga Bisanji Agarwal alias Haldiram Agarwal. He is the grandfather of Shri Shivkisan Agrawal, who was responsible for the fame and success of the sweet and savory products franchise. Moreover, he made the brand of Haldirams a household name in the Indian subcontinent.

Hotel Saravana Bhavan

Hotel Saravana Bhavan is the largest vegetarian restaurant chain in the world, founded in 1981 by Rajagopal, offers south Indian cuisine. They have more than 20 outlets in Chennai, 33 in India and 47 around the world (including USA, Canada, United Kingdom, France, Germany, Singapore, Malaysia, and the Middle East. There are plans to open 5-star Vegetarian-Hotels. This chain is also an example of successful model of Franchising.

Jumboking

Jumboking began its journey to brand the Vada Pav on 23rd August 2001. Jumboking in its 12th year of operations is a pioneer in the food retail company in India in the QSR (Quick Service Restaurants) segment.

Inspired by western models and applying it to Indian food, Jumbo King believes that the common man has the constitutional right to get hygienic food at an affordable price!

Jumboking has been founded by Dheeraj Gupta. Jumboking has a team of people spanning the functional areas of operations, business development, franchisee relations and marketing.

They have 51 operational outlets across India. It plans to put up a total of 500 stores by December 2018. Says Dheeraj Gupta, Founder and MD Jumboking: "We feel the Indian market can support more than 1000 Jumboking stores".

The company has appointed City Master Franchisees/single unit franchisees in Aurangabad, Mumbai, Banglore, Delhi, Indore, Raipur, Amravati, Goa, and Mysore.

Examples of other franchises which are taking India and the world by storm include Chi Kitchen & Bar (cuisine), Mahindra First Choice Wheels (used cars), Van Heusen (clothing), EduKart.com (education), Koutons Retail (fashion), The Yellow Chilli (restaurant chain) and VLCC (beauty and wellness).

Growth through mergers and acquisitions (M&A)

Mergers and Acquisitions (M&A) is a potential strategy for ensuring the accelerated growth of a business. There are various reasons that firms may choose to grow through M&A instead of expanding internally. The growth process is accelerated by acquiring a target in a line of business in which the bidding company wants to enlarge when compared with internal expansion, because the company already exists in place, with its own production capacity, distribution network and clientele. This saves a lot of time and investment for the growing company. Above all, growing through M&A may usually turn out to be less expensive compared with internal expansion, particularly when the replacement cost of assets is higher than the market value of target assets.

Mergers

A ***merger*** is a combination of two companies into one larger company. This action involves stock swap or cash payment to the target. In merger, the acquiring company takes over the assets and liabilities of the merged company. All the combining companies are dissolved and only the new entity continues to operate. In general, when the combination involves firms that are of similar size, the term, *consolidation,* is applied. When the two firms differ significantly by size, the term *merger* is used. Merger commonly **takes two forms**. In the first form *amalgamation,* two entities combine together and form a new entity, extinguishing both the existing entities. In the second form *absorption,* one entity gets absorbed into another. The latter does not lose its entity. Thus, in any type of merger at least one entity loses its entity.

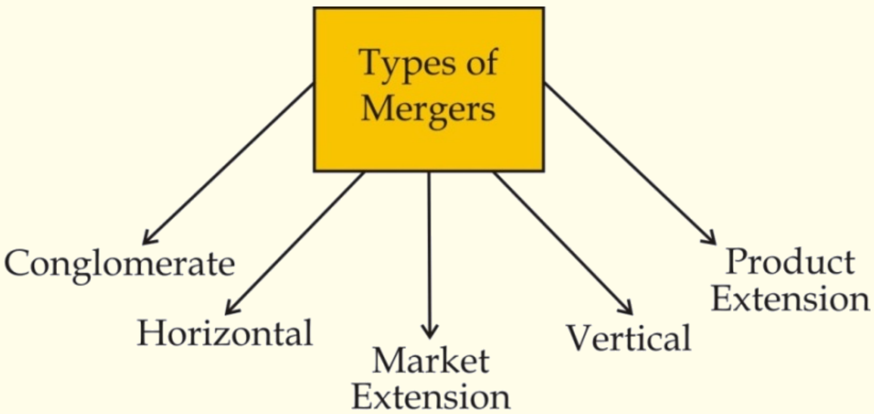
Hence, A + B = A, where company B is merged into company A (Absorption)

A + B = C, where C is an entirely new company (Amalgamation or Consolidation)

Usually, mergers occur in a consensual setting, where executives from the target company help those from the purchaser in a *due diligence* process to ensure that the deal is beneficial to both the parties. In a merger, the boards of directors of the two firms agree to combine and seek stockholder approval for the combination. In most cases, at least 50% of the shareholders of the target and the bidding firms have to agree to the merger. The target firm ceases to exist and becomes part of the acquiring firm.

For example, Digital Computers was absorbed by Compaq after it was acquired in 1997. The merger of TOMCO Ltd. with HLL is a classic example of absorption. In a consolidation, a new firm is created after the merger, and both the acquiring firm and the target firm stockholders receive stock in this firm; Citi Group, for instance, was created after the consolidation of Citicorp and Travelers Insurance Group.

Types of mergers



The term chosen to describe the merger depends on the economic function, purpose of the business transaction and relationship between the merging companies.

1. Conglomerate

A merger between firms that are involved in totally unrelated business activities. There are two types of conglomerate mergers: pure and mixed. Pure conglomerate mergers involve firms with nothing in common, while mixed conglomerate mergers involve firms that are looking for product extensions or market extensions.

Example: A leading manufacturer of athletic shoes merges with a soft drink firm. The resulting company is faced with the same competition in each of its two markets after the merger as the individual firms were before the merger. One example of a conglomerate merger was the merger between the Walt Disney Company and the American Broadcasting Company.

2. Horizontal merger

A merger occurring between companies in the same industry. Horizontal merger is a business consolidation that occurs between firms which operate in the same space, often as competitors offering the same goods or service. Horizontal mergers are common in industries with fewer firms, as competition tends to be higher and the synergies and potential gains in market share are much greater for merging firms in such an industry.

Example: A merger between Coca-Cola and the Pepsi beverage division, for example, would be horizontal in nature. The goal of a horizontal merger is to create a new, larger organization with more market share. If the merging companies' business operations are very similar, there may be opportunities to join certain operations, such as manufacturing and reduce costs.

3. Market extension mergers

A market extension merger takes place between two companies that deal in the same products but in separate markets. The main purpose of the market extension merger is to make sure that the merging companies can get access to a bigger market and that ensures a bigger client base.

Example: A very good example of market extension merger is the acquisition of Eagle Bancshares Inc. by the RBC Centura. Eagle Bancshares is headquartered at Atlanta, Georgia and has 283 workers. It has almost 90,000 accounts and looks after assets worth US $1.1 billion.

Eagle Bancshares also holds the Tucker Federal Bank, which is one of the ten biggest banks in the metropolitan Atlanta region as far as deposit market share is concerned. One of the major benefits of this acquisition is that this acquisition enables the RBC to go ahead with its growth operations in the North American market.

With the help of this acquisition RBC has got a chance to deal in the financial market of Atlanta , which is among the leading upcoming financial markets in the USA. This move would allow RBC to diversify its base of operations.

4. Product extension mergers

A product extension merger takes place between two business organizations that deal in products that are related to each other and operate in the same market. The product extension merger allows the merging companies to group together their products and get access to a bigger set of consumers. This ensures that they earn higher profits.

Example: The acquisition of Mobilink Telecom Inc. by Broadcom is a proper example of product extension merger. Broadcom deals in the manufacturing of Bluetooth personal area network hardware systems and chips for IEEE 802.11b wireless LAN.

Mobilink Telecom Inc. deals in the manufacturing of product designs meant for handsets that are equipped with the Global System for Mobile Communications technology. It is also in the process of being certified to produce wireless networking chips that have high speed and General Packet Radio Service technology. It is expected that the products of Mobilink Telecom Inc. would be complementing the wireless products of Broadcom.

5. Vertical merger

A merger between two companies producing different goods or services for one specific finished product. A vertical merger occurs when two or more firms, operating at different levels within an industry's supply chain, merge operations. Most often the logic behind the merger is to increase synergies created by merging firms that would be more efficient operating as one.

Example: A vertical merger joins two companies that may not compete with each other, but exist in the same supply chain. An automobile company joining with a parts supplier would be an example of a vertical merger. Such a deal would allow the automobile division to obtain better pricing on parts and have better control over the manufacturing process. The parts division, in turn, would be guaranteed a steady stream of business.

Synergy, the idea that the value and performance of two companies combined will be greater than the sum of the separate individual parts is one of the reasons companies merge.

Case Study-IV
Kraft's takeover of Cadbury

By Scott Moeller

The story: *In 2009, US food company Kraft Foods launched a hostile bid for Cadbury, the UK-listed chocolate maker. It became clear almost exactly two years later in August 2011, Cadbury was the final acquisition necessary to allow Kraft to be restructured and indeed split into two companies by the end of 2012: a grocery business worth approximately $16bn; and a $32bn global snacks business. Kraft needed Cadbury to provide scale for the snacks business, especially in emerging markets such as India. The challenge for Kraft was how to buy Cadbury when it was not for sale.*

The history

Kraft itself was the product of acquisitions that started in 1916 with the purchase of a Canadian cheese company. By the time of the offer for Cadbury, it was the world's second-largest food conglomerate, with seven brands that each generated annual revenues of more than $1bn.

Cadbury, founded by John Cadbury in 1824 in Birmingham, England, had also grown through mergers and demergers. It too had recently embarked on a strategy that was just beginning to show results. Ownership of the company was 49 per cent from the US, despite its UK listing and headquarters. Only 5 per cent of its shares were owned by short-term traders at the time of the Kraft bid.

The challenge

Not only was Cadbury not for sale, but it actively resisted the Kraft takeover.

Sir Roger Carr, the Chairman of Cadbury, was experienced in takeover defences and immediately put together a strong defensive advisory team. Its first act was to brand the 745 pence-per-share offer "unattractive", saying that it "fundamentally undervalued the company". The team made clear that even if the company had to succumb to an unwanted takeover, almost any other confectionery company (Nestlé, Ferrero and Hershey were all mentioned) would be preferred as the buyer. In addition, Lord Mandelson, then the UK's business secretary, publicly declared that the government would oppose any buyer who failed to "respect" the historic confectioner.

The response

Cadbury's own defence documents stated that shareholders should reject Kraft's offer because the chocolate company would be "absorbed into Kraft's low growth conglomerate business model – an unappealing prospect that sharply contrasts with the Cadbury strategy of a pure play confectionery company".

Little did Cadbury's management know that Kraft's plan was to split it into two to eliminate its conglomerate nature and become two more focused businesses, thereby creating more value for its shareholders.

The result

The Cadbury team determined that a majority of shareholders would sell at a price of roughly 830 pence a share. A deal was struck between the two chairmen on January 18 2010 at 840 pence per share plus a special 10 pence per share dividend. This was approved by 72 per cent of Cadbury shareholders two weeks later.

The key lessons

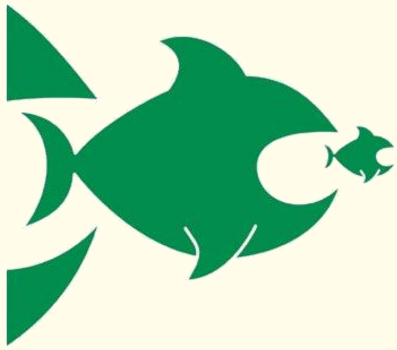
In any takeover, especially a cross-border deal in which the acquired company is as well known as Cadbury was in the UK, the transaction will be front-page news. In this case, it was the lead business story for at least four months. Fortunately, this deal had no monopoly or competition issues, otherwise those regulators could also have been involved.

But aside from any regulators, most other commentators will largely be distractions. It is important for the acquiring company's management and advisers to stay focused on the deal itself and the real decision-makers – the shareholders of the target company.

As this deal demonstrates, these shareholders may not (and often will not) be the long-term traditional owners of the target company stock, but rather very rational hedge funds and other arbitrageurs (in Cadbury's case, owning 31 per cent of the shares at the end), who are swayed only by the offer price and how quickly the deal can be completed.

Other stakeholders may have legitimate concerns that need to be addressed but this can usually be done after the deal is completed, as Kraft did.

Acquisitions



Acquisition is a more general term, enveloping in itself a range of acquisition transactions. It could be acquisition of control, leading to takeover of a company. It could be acquisition of tangible assets, intangible assets, rights and other kinds of obligations. They could also be independent transactions and may not lead to any kind of takeovers or mergers.

Meaning: A corporate action in which a company buys most, if not all, of the target company's ownership stakes in order to assume control of the target firm. Acquisitions are often made as part of a company's growth strategy whereby it is more beneficial to take over an existing firm's operations and niche compared to expanding on its own. Acquisitions are often paid in cash, the acquiring company's stock or a combination of both. An acquisition, also known as a *takeover,* is the buying of one company (the target) by another.

Types

There are four types of acquisitions:

1. **Friendly acquisition**

   Both the companies approve of the acquisition under friendly terms. There is no forceful acquisition and the entire process is cordial.

2. **Reverse acquisition**

   A private company takes over a public company.

3. **Back flip acquisition**

   A very rare case of acquisition in which the purchasing company becomes a subsidiary of the purchased company.

4. **Hostile acquisition**

   Here, as the name suggests, the entire process is done by force. The smaller company is either driven to such a condition that it has no option but to say yes to the acquisition to save its skin or the bigger company just buys off all its share, thereby establishing majority and hence initiating the acquisition.

Reasons for mergers and acquisitions

While one often hears CEOs saying that M & As are inspired by a desire to diversify or achieve higher growth rate, the reasons could be varied. Some of the commonly identified reasons are:

1. **Synergy**

   Synergy is the most essential component of mergers. In mergers, synergy between the participating firms determines the increase in value of the combined entity. In other words, it refers to the difference between the value of the combined firm and the value of the sum of the participants. Synergy accrues in the form of revenue enhancement and cost savings. For example, if firms A and B merge and the value of the combined entity—V(AB)—is expected to be greater than (VA+VB), the sum of the independent values of A and B, the combined entity is said to be benefitting through synergy.

Synergies between TATA Steel and Corus

There were a lot of apparent synergies between Tata Steel which was a low cost steel producer in fast developing region of the world and Corus which was a high value product manufacturer in the region of the world demanding value products. Some of the prominent synergies that could arise from the deal were as follows :

- *Tata was one of the low cost steel producers in the world and had self-sufficiency in raw material. Corus was fighting to keep its production costs under control and was on the lookout for sources of iron ore.*
- *Tata had a strong retail and distribution network in India and SE Asia. This would give the European manufacturer an in-road into the emerging Asian markets. Tata was a major supplier to the Indian auto industry and the demand for value added steel products was growing in this market. Hence, there would be a powerful combination of high quality development and low cost high growth markets.*
- *There would be technology transfer and cross-fertilization of R&D capabilities between the two companies that specialized in different areas of the value chain*
- *There was a strong culture fit between the two organizations, both of which highly emphasized on continuous improvement and ethics. Tata steel's Continuous Improvement Programme 'Aspire' with the core values: trusteeship, integrity, respect for individual, credibility and excellence. Corus's Continuous Improvement Programme 'The Corus Way' with the core values: code of ethics, integrity, creating value in steel, customer focus, selective growth and respect for our people.*

Synergy can take the following forms:

a) Operating synergy

This refers to the cost savings that come through economies of scale or increased sales and profits. It leads to the overall growth of the firm.

b) Financial synergy

This is the direct result of financial factors such as lower taxes, higher debt capacity or better use of idle cash. When a firm with accumulated losses or unabsorbed depreciation merges with a profitable firm and the combined firm can set off such losses against its profits, a financial synergy, known as tax shield, occurs. The following are some examples:

- When Hindustan Unilever Company acquired Lakme, it helped HUL to enter the cosmetics market through an established brand.

- When Glaxo and Smithkline Beecham merged, they not only gained market share but also eliminated competition between each other.
- Tata Tea acquired Tetley to leverage Tetley's international marketing strengths.

2. Acquiring new technology

To remain competitive, companies need to constantly upgrade their technology and business applications. To upgrade technology, a company need not always acquire technology. By buying another company with unique technology, the buying company can maintain or develop a competitive edge. A good example is a merger of a logistics company such as a land transport entity with an air-line cargo company. Another example is a merger between Blackberry and Treo which can incorporate cell phone capability and e–mail connectivity in one device; palm pilots and tablet laptops can provide benefits to both the entities.

3. Improved profitability

Companies explore the possibilities of a merger when they anticipate that it will improve their profitability. The results of the International Business Owners Survey, 2004, carried out by Grant Thompson, conducted across 26 countries in Europe, Africa, Asia-Pacific, and the US, showed that 34% of business use M&A to maintain or improve profitability. For example, European Media Group Betelsmann, Pearson, and others have driven their growth by expanding into the US though M&As.

4. Acquiring a competency

Companies also opt for M&A to acquire a competency or capability that they do not have and which the other firm does. For example, the ICICI ITC alliance made the retailer network and depositor base available to the merging entity. Similarly, IBM merged with Daksh for acquiring competencies that the latter possessed.

5. Entry into new markets

Mergers are often looked upon as a tool for hassle-free entry into new markets. Under normal conditions, a company can enter a new market, but may have to face stiff competition from the existing companies and may have to battle out for a share in the existing market. However, if the merger route is adopted, one can enter the market with greater case and avoid too much competition. For example, the merger of Orange, Hutch, and Vodafone took place to achieve this objective.

6. Access to funds

Often a company finds it difficult to access funds from the capital market. This weakness deprives the company of funds to pursue its growth objectives effectively. In such cases, a company may decide to merge with another company that is viewed as fund-rich. For example, TDPL (Tamil Nadu Dadha Pharmaceuticals) merged with Sun Pharma since TDPL did not have funds to launch new products.

7. **Tax benefits**

Mergers are also adopted to reduce tax liabilities. By merging with a loss-making entity, a company with a high tax liability can set off the accumulated losses of the target against its profits gaining tax benefits. For example, Ashok Leyland Information Technology (ALIT) was acquired by Hinduja Finance, a group company, so that it could set off the accumulated losses in ALITs books against its profits.

Reasons for failure of merger and acquistions

While there is often a great hype when a merger or acquisition is announced, the end result is not always positive. The most common reasons for failure are as follows:

1. **Unrealistic price paid for target**

The process of M&A involves valuation of the target company and paying a price for taking over the assets of the company. Quite often one finds that the price paid to the target company is much more than what should have been paid. While the shareholders of the target company stand benefited, the shareholders of the acquirer end up on the losing side. This is because they have to carry the burden of the overpriced assets of the target company which dilutes the future earnings of the acquirer. Having bid over-enthusiastically, the buyer may find that the premium paid for the acquired company's shares, the so-called 'winner's curse' wipes out any gains made from the acquisition.

This phenomenon is generally noticed in the later years when the acquirer has to revalue the assets and write goodwill booked at the time of M&A.

2. **Difficulties in cultural integration**

Every merger involves combining of two or more different entities. These entities reflect different corporate cultures, styles of leadership, differing employee expectations and functional differences. If the merger is implemented in a way that does not deal sensitively with the companies people and their different corporate cultures, the process may turn out to be a disaster. There may be acute contrasts between the attitudes and values of the two companies, especially if the new partnership crosses national boundaries. While the process is being executed, these differences are known but often ignored. As years pass by and the combined entity tries to synergize the operations, these differences surface and often lead to failure of the merger. For example, the merger of Daimler Benz with Chrysler. While Daimler-Benz's culture stressed on a more formal and structured management style, Chrysler favoured a more relaxed, freewheeling style.

3. **Overstated synergies**

Mergers and acquisitions are looked upon as an important instrument for creating synergies through increased revenue, reduced costs and reduction in networking capital and improvement in the investment intensity. Overestimation for these can lead to failure of mergers.

4. Integration difficulties

Companies very often face integration difficulties, i.e., the combined entity has to adapt to a new set of challenges given by the changed circumstances. To do this, the company prepares plans to integrate the operations of the combining entities. If the information available on related issues is inadequate or inaccurate, integration becomes difficult.

5. Poor business fit

Mergers and acquisitions also fail when the products or services of the merging entities do not naturally fit into the acquirer's overall business plan. This delays efficient and effective integration and causes failure.

6. Inadequate due diligence

Due diligence is a crucial component of the M&A process as it helps in detecting financial and business risks that the acquirer inherits from the target company. Inaccurate estimation of the related risk can result in failure of the merger.

7. High leverage

One of the most crucial elements of an effective acquisition strategy is planning how one intends to finance the deal through an ideal capital structure. The acquirer may decide to acquire the target through cash. To pay the price of acquisition, the acquirer may borrow heavily from the market. This creates a very high leveraged structure and increases the interest burden of the company. This increased interest cost may consume a big portion of the earnings and defeat the very purpose of acquisition.

8. Boardroom split

When a merger is planned, it is crucial to evaluate the composition of the boardroom and compatibility of the directors. Managers or directors who are suddenly deprived of authority can be particularly bitter. Specific personality clashes between executives in the two companies are also very common. This may prove to be a major problem, slowing down or preventing integration of the entities.

9. Regulatory issues

The entire process of merger requires legal approvals. If any of the stakeholders are not in favour of the merger, they might create legal obstacles and slow down the entire process. This results in regulatory delays and increases the risk of deterioration for the business. While evaluating a merger proposal, care should be taken to ensure that regulatory hassles do not crop up.

10. Human resources issues

A merger or acquisition is identified with job losses, restructuring and the imposition of a new corporate culture and identity. This can create uncertainty, anxiety and resentment among the company's employees. Companies often pay undue attention to the short term legal and financial considerations involved in a merger or acquisition, and neglect crucial HR issues related to corporate identity and communication, which in turn impact the worker's morale and productivity. These HR issues are crucial to the success of M&As.

B. Value addition

Business add values to goods and services by modifying them in a particular way to create a new product of greater value to customers.

Added value, from a financial point of view, represents the difference between the value of goods and services that are used as inputs to a production process and the value of the outputs of that process.

Added value, from a marketing perspective, means adding value that turns a commodity into a branded product. Branded products and services can also have value added by enhancing their design, characteristics or range of features.

Commodities are basically unprocessed raw products such as crude oil, meat carcasses, fresh fruit and cotton balls. To add value to a commodity, it needs to be processed in some way to turn it into a branded product that consumers are willing to pay more for than the raw product. For example, a food processor could purchase milk from a dairy farmer and make it into cheese. The packaged cheese has added value and becomes a branded good.

The value people place on goods and services determine the quantitative value (the money people are willing to exchange for the product) and the qualitative value (the desirability of the product).

Common examples of adding value include:

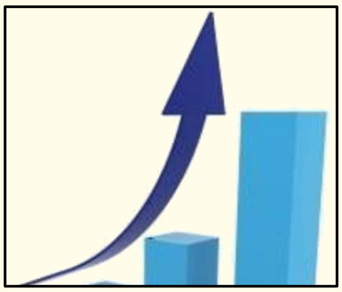
- Turning cotton into fabric
- Turning milk into cheese
- Packaging ready-to-use grated cheese into serving size packets
- Turning wood into paper
- Designing a mobile phone that can also take photographs
- Fortifying food with vitamins and minerals

Adding Value is a Business Strategy for Growth (Kevinzhengli)

Types of added value

There are several types of added values that a business can employ to improve its products and services.

- Quality
- Environmental



Value based growth

- Cause-related
- Cultural

The different types of added value are not mutually exclusive and can be employed at any phase of the production or service cycle.

1. Quality added value

Quality added value is basically adding convenience, ease of use or other desirable characteristics that customers value. For example, turning a commodity into a branded product or design enhancements like pull tabs for easy opening or sipper tops on beverage bottles.

2. Environmental added value

Environmental added value employs methods or systems that do not harm the environment or are less harmful than those commonly used. For example, using less electricity, using less fuel and using recycled material for packaging.

3. Cause-related added value

Cause-related added value is a social marketing strategy where business contributes part of the revenue from a product or service to a cause. For example, a business may donate a percentage of revenue from each transaction to a cause such as an educational facility for disadvantaged children or a wildlife sanctuary.

4. Cultural added value

Cultural added value is also a social marketing strategy that employs methods or systems of production involving cultural aspects or allow for the needs and sensitivities of cultural groups. For example, producing kosher food (in accord with Jewish law) or using a combination of English and the language of other ethnic groups in a community in written communications.

Adding value can be used as a marketing strategy to differentiate a product from competing products. Such strategies should be fully researched and included in a business plan to show the potential benefits to a business.

C. Moving-up the value chain

A value chain is the whole series of activities that create and build value at every step. The total value delivered by the company is the sum total of the value built up all throughout the company. Michael Porter developed this concept in his 1980 book 'Competitive Advantage'. In simple words **'Value Chain'** is a high level model of how business receive raw-materials, add value to the raw-materials through various processes and sell as finished products to customers. 'Value Chain' analysis looks at every step of business, from raw-materials to the eventual end users, with one goal to deliver maximum value.

Michael Porter introduced the value chain analysis concept in his 1985 book ‘The Competitive Advantage’. Porter suggested that activities within an organisation add value to the service and products that the organisation produces and all these activities should be run at optimum level if the organisation is to gain any real competitive advantage. If they are run efficiently, the value obtained should exceed the costs of running them i.e. customers should return to the organisation and transact freely and willingly. Michael Porter suggested that the organisation is split into 'primary activities' and 'support activities'.

Primary activities

Inbound logistics: Goods being obtained from the organisation's suppliers and to be used for producing the end product.

Operations: Raw materials and goods are manufactured into the final product. Value is added to the product at this stage as it moves through the production line.

Outbound logistics: Once the products have been manufactured, they are ready to be distributed to distribution centres, wholesalers, retailers or customers. Distribution of finished goods is known as outbound logistics.

Marketing and sales: Marketing must make sure that the product is targeted towards the correct customer group. The marketing mix is used to establish an effective strategy, any competitive advantage is clearly communicated to the target group through the promotional mix.

Services: After the product/service has been sold, what support services does the organisation offer customers? This may come in the form of after sales training, guarantees and warranties.

With the above activities, any or a combination of them are essential if the firm has to develop the "competitive advantage" which Porter talks about in his book.

Support activities

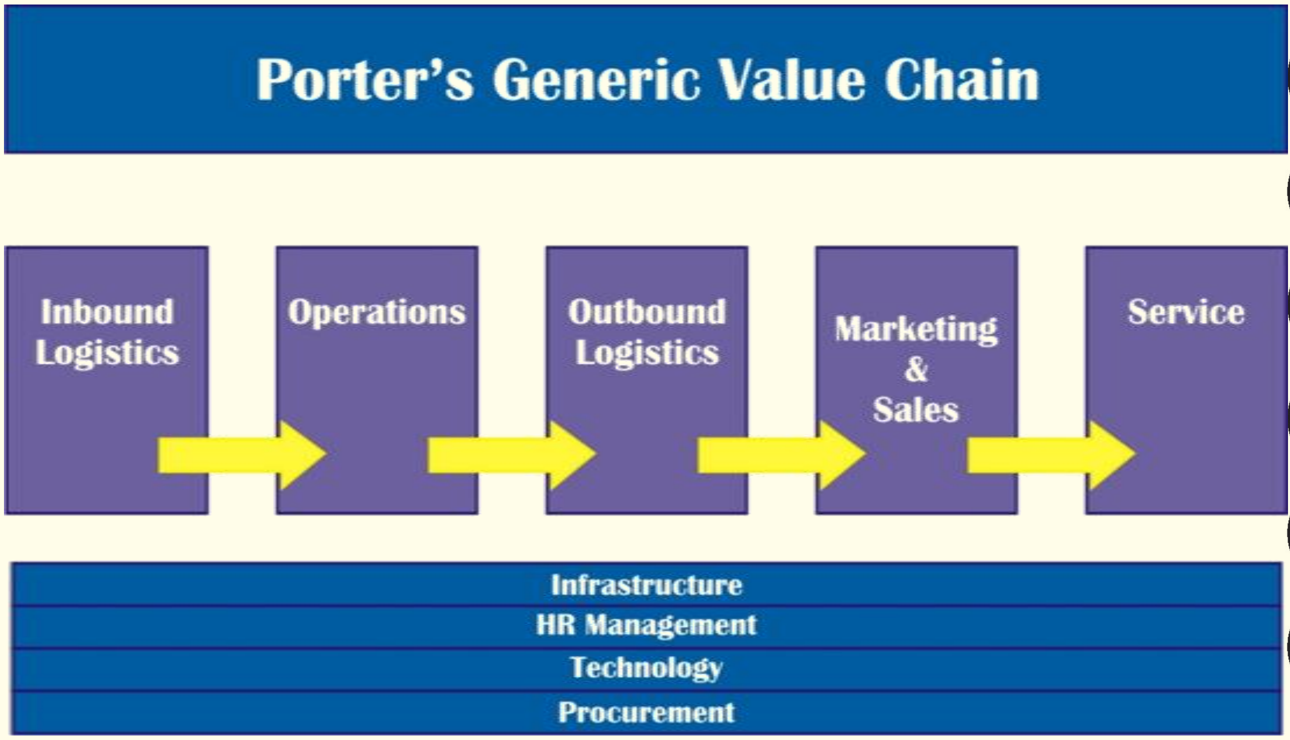
Support activities assist the primary activities in helping the organisation achieve its competitive advantage. They include:

Procurement: This department must source raw materials for the business and obtain the best price for doing so. The challenge for procurement is to obtain the best possible quality available (on the market) for their budget.

Technological development: The use of technology to obtain a competitive advantage is very important in today's technology driven environment. Technology can be used in many ways, including production, to reduce cost and thus adding value, research and development to develop new products on the internet so that customers can have 24/7 access to the firm.

Human resource management: The organisation will have to recruit, train and develop the right people for the organisation to be successful. Staff will have to be motivated and paid the 'market rate', if they are to stay with the organisation and add value. Within the service sector such as the airline industry, employees are at the competitive advantage as customers are purchasing a service, which is provided by employees; there isn't a product for the customer to take away with them.

Firm infrastructure: Every organisation needs to ensure that their finances, legal structure and management structure work efficiently and help drive the organisation forward. Inefficient infrastructure's waste resources could affect the firm's reputation and even leave it open to fines and sanctions.



Six requirements for value chain management

Value chain managers are always looking for ways to improve the company's processes.

1. **Coordination and collaboration**

   To increase efficiency within an organization, coordination and collaboration is essential. Coordinate work groups to ensure efforts are not duplicated. Utilize the theory that the whole is greater than the sum of its parts by collaborating with other groups and individuals to achieve a common goal.

2. **Technology investment**

   Technology plays a large role in manufacturing and distribution. With outdated technology, such as old computers or machinery, an organization's competitiveness is weakened due to a loss in productivity.

3. **Organizational process**

   In value chain management, every aspect of an organization's process is identified. Improvement in processes through better technology and greater procedural knowledge is important to the present and future success of a company.

4. **Leadership**

   Strong leaders are crucial to the success in value chain management. Good leaders earn the respect of their employees through sound management practices. Conflict management, motivation and direction are traits that strong leaders display.

5. **Employee/human resources**

A central hub of information on benefits, company policies, hiring and conflict management is also necessary for a corporation to function properly. Without a knowledgeable and active human resources department, employees may feel they don't have a voice within the company. Many times, an employee is hesitant to go directly to the supervisor with issues; a human resources employee can act as a liaison in many situations.

6. **Organizational culture and attitudes**

Organizations that foster strong cultural identity with positive attitudes tend to attract and retain top employees. Regular corporate sponsored activities are suggested to help build cultural unity and keep attitudes positive while boosting productivity.

SUMMARY

- *Growth of an enterprise can be either through a. internal expansion or b. external expansion*
- *Main forms of external expansion are :*

  a. Franchising; b. merger; c. acquisition
- ***Franchising** is "an arrangement whereby the manufacturer or sole distributor of a trademarked product or service gives exclusive rights of local distribution to independent retailers in return for their payment of royalties and conformance to standardized operating procedures".*
- ***Four types of franchising***
  - *a. Product franchise business opportunity*
  - *b. Manufacturing franchise opportunity*
  - *c. Business franchise opportunity ventures*
  - *d. Business format franchise opportunity*
- ***Advantages to the franchisee***
  - *Product acceptance*
  - *Management expertise*
  - *Capital requirements*
  - *Knowledge of the market*
  - *Operating and structural controls*
- ***Advantages to the Franchisor***
  - *Quick expansion*
  - *Cost advantages*
- ***Disadvantages to the franchisee***
  - *Right and the only way of doing things*
  - *Continuing cost implication*
  - *Risk of franchisor getting bought*
  - *Inability to provide services*
- ***Disadvantage to the franchisor***

  Difficulty in finding quality franchisee's
- *A **merger** is a combination of two companies into one larger company.*

- ***Types of mergers:***

  1. Conglomerate; 2. Vertical; 3. Market extension; 4. Horizontal; 5. Product extension

- ***Acquisition***

  It is a corporate action in which a company buys most, if not all, of the target company's ownership stakes in order to assume control of the target firm.

- *Acquisitions are often made as part of a company's growth strategy whereby it is more beneficial to take over an existing firm's operations and niche compared to expanding on its own.*

- *Acquisitions are often paid in cash, the acquiring company's stock or a combination of both. An acquisition, also known as a takeover, is the buying of one company (the target) by another.*

- ***Types of acquisition***

  a. Friendly acquisition; b. Reverse acquisition; c. Back flip acquisition; d. Hostile acquisition

- ***Reasons for mergers and acquisitions***
  - *Synergy - operating synergy and financial synergy*
  - *Acquiring new technology*
  - *Acquiring a competency*
  - *Access to funds*
  - *Improved profitability*
  - *Entry into new markets*
  - *Tax benefits*

- ***Reasons for failure of merger and acquistions***
  - *Unrealistic price paid for target*
  - *Overstated synergies*
  - *Inconsistent strategy*
  - *Inadequate due diligence*
  - *Boardroom split*
  - *Human resource issues*
  - *Difficulties in cultural integration*
  - *Integration difficulties*
  - *Poor business fit*
  - *High leverage*
  - *Regulatory issues*

- ***Value addition***

  Businesses add value to goods and services by modifying them in a particular way to create a new product of greater value to customers.

- ***Types of added value***
  - *Quality*
  - *Cause-related*
  - *Environmental*
  - *Cultural*

- ***Value Chain**: It is the whole series of activities that create and build value at every step.*

  Michael Porter introduced the value chain analysis concept in his 1985 book 'The Competitive Advantage'. Porter suggested that activities within an organisation add value to the service and *products that the organisation produces, and all these activities should be run at optimum level if the organisation is to gain any real competitive advantage. If they are run efficiently, the value obtained should exceed the costs of running them i.e. customers should return to the organisation and transact freely and willingly.*

- *Michael Porter suggested that the organisation is split into 'primary activities' and 'support activities'.*
- ***Primary activities***

  1. Inbound logistics; 2.Operations; 3.Outbound logistics; 4. Marketing and sales; 5. Services
- ***Support activities***

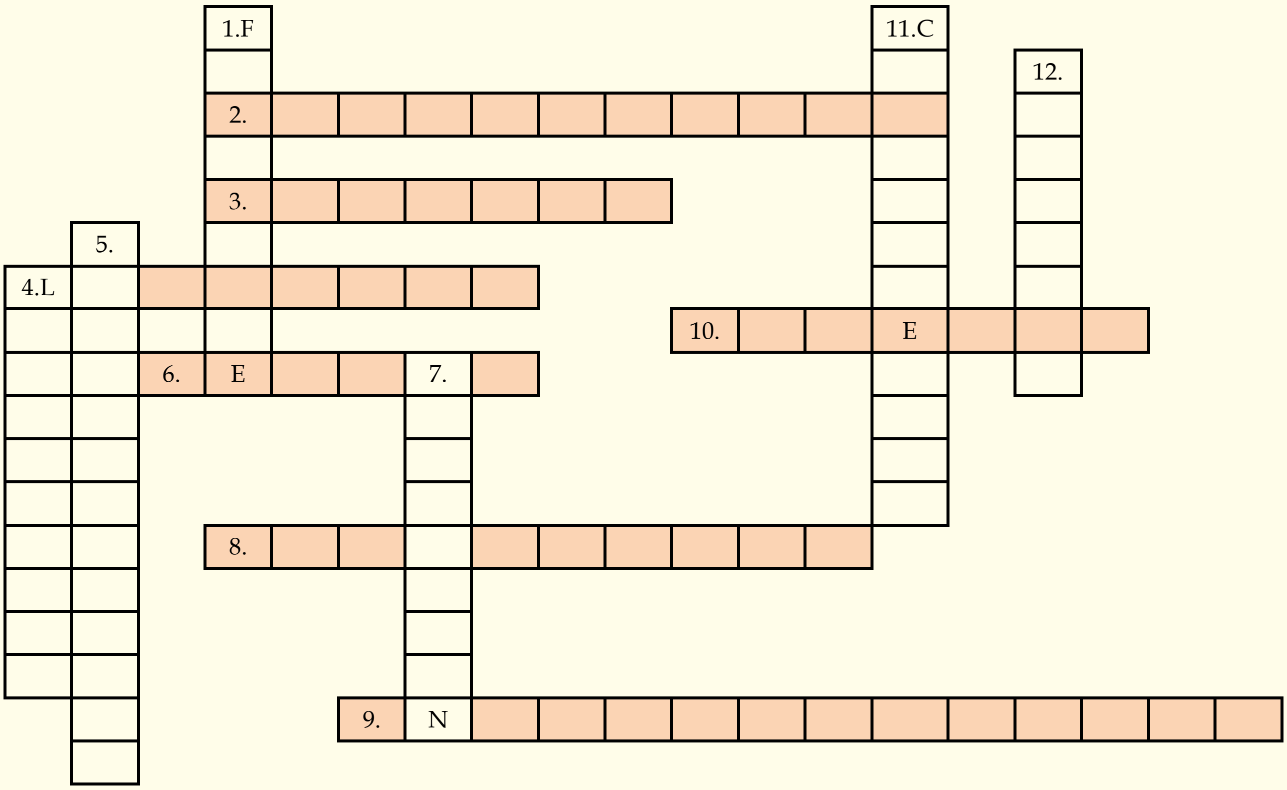
  1. Procurement 2. Technology development 3. Human resource management 4. Firm infrastructure
- ***Six requirements for value chain management***

  1. Coordination and Collaboration 2. Technology Investment 3. Organizational Process 4. Leadership 5. Employee/Human Resources 6. Organizational Culture and Attitudes

"The price of success is hard work, dedication to the job at hand, and the determination that whether we win or lose, we have applied the best of ourselves to the task at hand."

- Vince Lombardi

REVIEW CROSSWORD PUZZLE



Across:

2. A corporate action in which a company buys most, if not all, of the target company's ownership stakes in order to assume control of the target firm
3. The way of life of the people
4. The management of the flow of goods between the point of origin and the point of consumption in order to meet some requirements
6. A combination of two companies into one larger company
8. The company that allows an individual (known as the franchisee) to run a location of their business
9. The basic physical and organizational structures and facilities
10. It refers to the difference between the value of the combined firm and the value of the sum of the participants

Down:

1. McDonald's works under this arrangement
4. The action of leading a group of people
5. The action of working with someone to get something done
7. The action of becoming larger or more extensive
11. A company that comprises multiple different corporations.
12. The use of various financial instruments or borrowed capital, such as margin, to increase the potential return of an investment.

LET'S REVISE

A. Answer each of these questions in about fifteen words:

1. What are the two ways in which an organization can expand?
2. Who is a franchisor?
3. Who is a franchisee?
4. What is franchising?
5. Which is the most popular form of franchising?
6. What is acquisition?

B. Answer each of these questions in about fifty words:

1. Explain in brief the three ways in which an organization can expand externally.
2. Enumerate the importance of franchising.
3. Differentiate between consolidation and merger.
4. Name the two forms that merger can take place.
5. Explain the types of acquisition.
6. What is value addition? Explain by giving examples.

C. Answer each of these questions in about one hundred and fifty words:

1. Explain the types of franchising.
2. What are the disadvantages of franchising to the franchisee?
3. What is synergy? In what forms can it take place?
4. What are the different types of value added?

D. Answer each of these questions in about two hundred and fifty words:

1. Explain the advantages of franchising, both for the franchisor and franchisee
2. Explain in detail the types of mergers
3. What do you think are the reasons for failure of merger and acquisition?
4. What is meant by moving up the value chain? Explain with the help of an example.
5. Explain in detail Porter's Generic Value Chain with the help of a diagram.
6. Explain the requirements for value chain management.

E. HOTS (High Order Thinking Skills)

In the following cases identify the type of merger:

a) A merger between firms that are involved in totally unrelated business activities.

b) A merger occurring between companies in the same industry.

c) It takes place between two companies that deal in the same products but in separate markets.

d) It takes place between two business organizations that deal in products that are related to each other and operate in the same market.

e) It is between two companies producing different goods or services for one specific finished product.

F. Application Based Questions

1. ABC Company, manufacturing shoes, has taken over XYZ Company which also manufactures shoes at a small scale. What do you think will be the reason for this kind of takeover?
2. Vimal Company Ltd., were earlier producing pencils, now they have decided to further venture into the field of notebooks and paper. What do you think is the company attempting to do? Identify and explain the concept.

G. Activities

1. Look around in the market for a product of your interest. Suggest some ways in which the company can move up their value chain.
2. Find out in your area if there are any shops which are run on the franchise model and assess the success of those firms.
3. Make a list of major companies which have merged or have acquired some other company and state whether they are successful or unsuccessful, giving reasons.

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