Latin American franchise internationalization: The impact of institutional environment

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We analyze the internationalization of Brazilian franchise chains in Latin America. A total of 119 observations verify international commitment in each country in relation to institutional environment factors and how they are moderated by chain size and industry. The results show that despite all institutional aspects having a significant effect, their explanatory power depends on chain size. Larger franchise chains usually choose countries with better institutional aspects in terms of contract compliance and business freedom, even if the efficiency of business conditions in these countries are not the best in Latin America. In this study, were used public data from international organizations that report on the ease of doing business, level of corruption, political risk, and legal regulations. Specifically, it contributes by using institutional theory in franchising in order to understand the process of chain internationalization originating from emerging markets. Our results, in part, contradict the idea that the origin disadvantage is always an advantage of internationalization.

KEYWORDS
country analysis, emerging markets, entrepreneurship, franchise chains, franchise internationalization, institutional theory

1 | INTRODUCTION

The internationalization of franchise chains had as its precursor North American franchise chains directed toward the developed markets of Europe, Canada, Australia, and East Asia. In the current decade, due to growth in emerging markets, a second wave of internationalization of North American chains in these markets has been present (Aliouche & Schlientrich, 2011; Baena, 2012; Dant & Grünhagen, 2014). The inverse path has also occurred; that is, franchise chains from emerging countries have sought to expand into international markets (Alon, 2004; Castrogiovanni & Vozikis, 2000; Dant, Perri-got, & Cliquet, 2008; Grünhagen, Dant, & Zhu, 2012; Grünhagen, Witte, & Pryor, 2010; Wang, Zhu, & Terry, 2008; Welsh, Alon, & Falbe, 2006). As a result of this late internationalization and, in particular, country of origin, the study of these chains is seen as worthy research (Dant & Grünhagen, 2014). Predominant franchise theories are based on American franchises (Dant, Grunhagen, & Windsperger, 2011); however, franchise chains from emerging countries have different historical, economic, social, and cultural perspectives and competitive contexts to American franchises, instilling a need for new theoretical lenses (Dant & Grünhagen, 2014; Dant et al., 2011).

Institutional theory and national culture theory have the potential for academic exploration when understanding the internationalization of franchise chains originating from emerging countries (Jell-Ojobor & Windsperger, 2014; Merrilees, 2014), especially for understanding entrepreneurship in emerging markets (Alon & Rottig, 2013; Goyal, McCord, & Kappor, 2017). As the emerging context differs from the developed, the success of strategies in international markets stems from a considerable understanding of the institutional environment of these countries (Elango & Lahiri, 2014; Goyal, McCord, & Kappor, 2017; Kogut, 2003; Peng, Sun, Pinkham, & Chen, 2009). The literature recognizes differences in behavior in formal and informal institutions of emerging and developed countries (Kamoche & Harvey, 2006; London & Hart, 2004; Meyer, 2004; Ramamurti, 2004). As emerging-market firms face more institutional difficulties in their home markets, they can capitalize on this disadvantage by turning it into a nonlocal capability (Rugman & Verbeke, 2001) and gain advantages when operating in other emerging markets with institutional barriers (Cuervo-Cazurra, 2006; Cuervo-Cazurra & Genc, 2008; Ghemawat & Khanna, 1998) and institutional gaps (Khanna & Palepu, 2010).

Given the concept that using disadvantage as a nonlocal capability in order to exploit other emerging countries, franchises should be...
assessed with some caveats. The franchise system is a partnership between franchisor and franchisee that is mediated by a contract between the parties. Thus, the fulfillment of contracts (enforcing contracts) and the regulations under which they are established (business freedom) cannot follow a pattern of better or worse. This means that—taking certain particularities of some formal institutions—certain inefficiencies in a host country (e.g., political stability, corruption, business environment efficiency) can be an advantage for franchises coming from emerging countries. However, others related exclusively to contracts may, in fact, be an obstacle to extension. In this article, we support the thesis that in relation to aspects of institutional environments, the internationalization of emerging franchises to other emerging countries is associated with institutional security related to contracts and regulations as well as with institutional insecurity of other institutional aspects, such as corruption, political stability, and institutional environment. These dimensions were selected in accordance with their presence in other studies (Aliouche & Schlentrich, 2009, 2011; Baena, 2012; Baena & Cerviño, 2014; Hoffman, Munemo, & Watson, 2016; Melo, Borini, Oliveira, & Parente, 2015), showing their importance in the internationalization and operationalization of franchise chains.

To test our hypotheses, we analyze the internationalization of Brazilian franchise chains in Latin America. A total of 119 observations verify international commitment in each country (number of franchises in each country) in relation to institutional environment factors and how they are moderated by chain size and industry. The results show that despite all institutional aspects having a significant effect, their explanatory power depends on chain size. Larger franchise chains usually choose countries with better institutional aspects in terms of contract compliance and business freedom, even if the efficiency of business conditions in these countries is not the best in Latin America.

These research results contribute to studies on the internationalization of franchise chains in a macro perspective, involving origin and destination countries (Alon, 2006; Castrogiovanni & Vozikis, 2000; Dant & Grünhagen, 2014; Grünhagen et al., 2010; Merrilees, 2014; Hoffman & Preble, 2004; Welsh et al., 2006). Specifically, it contributes by using institutional theory in franchising (Hoffman et al., 2016; Merrilees, 2014; Jell-Ojobor & Windsperger, 2014) in order to understand the process of chain internationalization originating in emerging markets. In addition, we are looking from a perspective of emerging-market firms accessing other emerging countries (i.e., South–South), which is different for other previous studies that have focused on developed countries accessing emerging markets (i.e., North–South) such as the case of Spanish firms in Latin America (Baena, 2012, 2015; Baena & Cerviño, 2014).

2 | LITERATURE REVIEW

2.1 | Institutional environments and the internationalization of franchising

Literature on international business, especially when it follows an institutional perspective, has shown a strong commitment to characterize the particularities of emerging-market firms in order to explain their internationalization process. To understand the strategic choices involved in international markets, it is important to analyze problems and institutional gaps faced by these firms (Elango & Lahiri, 2014; Peng et al., 2009; Peng, Wang, & Jiang, 2008). Consequently, some internationalization studies on franchising have proliferated under an institutional perspective.

The first studies on institutional environments for franchise chains date back to the internationalization processes undertaken by U.S. chains in the 1990s (Castrogiovanni & Vozikis, 2000; Hoffman & Preble, 2004). Entrance with the franchise model in emerging markets aimed to meet an intense unpreparedness of local shopkeepers with infrastructure (Castrogiovanni & Vozikis, 2000). However, entry into these markets proceeded cautiously because American franchises prioritized international environments with cultural characteristics similar to their own (Hoffman & Preble, 2004). As such, chains have a predilection for entry using the master franchising method in environments that have high political risk, competition, and cultural and demographic distances (Alon, 2006; Aliouche & Schlentrich, 2009, 2011). Geographic distance, political instability, and corruption are major barriers to business in emerging markets (Baena, 2012, 2015). For example, Spanish franchises in Latin America often maintain franchisor–franchisee relationships marked by nonstandard and personalized behavior, something not expected in this type of structural arrangement (Baena, 2012; Baena & Cerviño, 2014). However, despite institutional difficulties, economic growth in these markets seems to prevail when choosing destination countries (Hoffman et al., 2016). One of these examples is Brazil, the largest market in Latin America, even in the face of typical institutional constraints of an emerging market that are particularly attractive to foreign companies (Gouvea, 2004; Gouvea, Kapelianis, & Montoya, 2016).

The research above presents some origin bias, as the analysis is restricted to American franchises and, at most, extends to franchises originating in developed European countries (Aliouche & Schlentrich, 2009, 2011; Baena, 2012, 2015). Questions and behavior can be expanded to franchises outside this focus, specifically to those originating in emerging countries (Dant et al., 2011; Merrilees, 2014).

From the few existing studies, it can be seen that there are some similarities between franchises originating in developed and developing countries. Taking Brazil as an example, similarities occur through both personal relations and the apparent lack of systematic performance in international markets (Melo et al., 2015; Rocha et al., 2014). On the other hand, taking into account the issues of demographics and economic, political, and legal environments, results show a predominance of operations in Latin American and emerging countries, but with a spread of international operations in markets with heterogeneous environments, which can increase international management complexity for franchise chains (Melo et al., 2015).

However, it must be reaffirmed that the specific impact of institutional aspects of destination countries in franchise chain internationalization originating in an emerging market has been ignored. Consequently, it is questionable whether the extension of the origin disadvantage assumption has the chance to become a nonlocal capability in other emerging countries (Cuervo-Cazurra & Genc, 2008). Caveats about the structural particularities of the franchising system
for some aspects, such as regulation and contracts, would generate insecurity and derail business. Given this issue, in the next section we develop arguments about how unstable institutional environments can be an advantage for franchises of emerging markets.

3 | HYPOTHESIS DEVELOPMENT

Initially in this section, we comment on institutional aspects that are essential to the operation of the franchise (contracts and regulation), which differ in the view that inefficiency and ineffectiveness can be an advantage for emerging-market franchises. It argues that the factors in this inversion of values could be an advantage for franchises of emerging countries when operating in emerging-market destinations. The choice of factors (political instability, corruption, and market inefficiency) is due to their being institutional aspects (here we are not analyzing cultural aspects) that were prevalent in studies of franchise internationalization and institutional environments (Aliouche & Schlientrich, 2009, 2011; Baena, 2012; Baena & Cerviño, 2014; Grünhagen et al., 2010; Hoffman et al., 2016; Melo et al., 2015). Figure 1 shows the conceptual framework that guides our argumentation.

3.1 | Cost of enforcing contracts

We begin our discussion with contracts, which are a central factor that establishes the franchising system. The legal conditions of countries affect entrepreneurial activities, with entrepreneurs establishing contracts that require judicial decisions that are dependent on the fulfillment of law. Such legal standards for the protection of entrepreneurs are subject to variation in accordance with the degree of seriousness of legal institutions in a country (Herrera-Echeverri, Haar, & Estévez-Bretón, 2014). Particularly in the business environment, ensuring the execution of contracts and property protection leads to success in agreement with the power of the execution of law in a country (Aidis, Estrin, & Mickiewicz, 2012; Kaufmann, Kraay, & Mastruzzi, 2010).

Property rights comprise the legal principles of protection for businesses and are understood in various parameters: (a) the power of government influence in the judicial system; (b) commercial codes defined in contracts; (c) arbitration in international negotiations; (d) expropriation of property by the government; (e) corruption in the judiciary; (f) processing time of judicial sentences; (g) guaranteed legality; and (h) protection of private property (Heritage Foundation, 2014). Countries with strong property rights inhibit the arbitrary action of governments, stakeholders, and entrepreneurs, especially in terms of obstructions that may slow business (Harper, 2003; Hodler, 2009).

That said, it is assumed that the legal aspects of a country, when fortified, promote economic development that supports businesses. This occurs because there are greater guarantees of protection for entrepreneurs, investors, and business partners and, thus, reduces opportunistic maneuvers that occur in commercial relationships (Herrera-Echeverri et al., 2014; Parker, 2007; Svensson, 1998). In markets with weak legal protection, there is little incentive for honest behavior, and entrepreneurs are influenced to adapt to current business practices in these markets in order to continue their endeavors. There is little loyalty and respect in market competition, which affects entrepreneurial activity and promotes predatory activities (Aidis, Estrin, & Mickiewicz, 2008; Aidt, 2009; Henrekson, 2007; Hodler, 2009).

In international markets where efficiency and transparency in legal systems exist, it leads to reduced transaction costs. These are important criteria for attracting investors to a particular country, given that the laws promote higher security. However, emerging markets notoriously have greater weaknesses in legal compliance than in developed markets (Denis & McConnell, 2003; Thenmozhi & Narayanan, 2016). Therefore, it is expected that franchise chains of emerging markets deal daily with legal limitations in their destination countries. However, in international operations, dealing with these obstacles or unstable situations can become very costly and create complex relationships with franchisees. Such institutional environment weakness can favor franchisees more than franchisors. Therefore, we propose the following research hypothesis:

Hypothesis 1: Emerging countries with lower contract implementation costs are associated with greater commitment by franchise chains of emerging countries.
3.2 | Business freedom

The administrative environment of a country can be understood as the market conditions for opening and maintaining a business. In the case of international operations in a destination country, such an environment, when conducive to business, generates greater entrepreneur confidence (Berry, Guillén, & Zhou, 2010). As such, the existence of regulations to facilitate access to credit for private financing constitutes a relevant element for the opening and prosperity of businesses (Di Patti & Dell’Ariccia, 2004). In this administrative environment, the regulation of business by bureaucratic procedures involves time and difficulty, namely, hiring employees, importing and exporting, opening new businesses, and the degree of market openness (Berry et al., 2010).

In international markets, there are changes in regulations that create barriers to business activity, resulting in a certain instability for entrepreneurs that discourage such action (Miller & Kim, 2013). In other words, the market becomes unfavorable to business freedom, that is, market characteristics in relation to business activities carried out by private entities as well as interference by regulations imposed by governments. Barriers do not reside within excessive business regulation but in the quality of these regulations in terms of fostering entrepreneurial activity (Cebula, Rossi, & Clark, 2016).

Therefore, rather than excessive regulations, it is important that a country has quality business regulations to foster entrepreneurial activity. Highly regulated markets and bureaucratic imperatives hinder entrepreneurial activity for both the opening and expansion of business (Klapper, Laeven, & Rajan, 2006; Parker, 2007). In turn, quality regulations for the creation of business, labor procedures, and financial and financial issues have effects related to increases in entrepreneurial activity in a country (Van Stel, Storey, & Thurik, 2007). In markets that have lower barriers to business, higher rates of economic growth, productivity, employment, and especially the encouragement of entrepreneurial activity can be seen (Belasen & Hafer, 2013; Nikoluev, Hall, Pulito, & Van Metre, 2013).

Thus, even for franchises from emerging markets, excessive regulation and poor-quality relationships create a business environment without the certainty of business realization or investment freedom. Then, in host countries with conditions far short of regulations governing business, there is no way for franchises to capitalize on this disadvantage as a nonlocal capacity. The company could not be against legal regulation, which is something coercive. This leads us to propose that:

**Hypothesis 2:** Emerging countries with higher levels of business freedom are associated with greater commitment of franchise chains from emerging markets.

3.3 | Political stability

Host countries that have stable political environments are conducive to doing business, as such environments favor long-term relationships between businesses and governments (Magnusson, Westjohn, Gordon, & Aurand, 2012). The institutional characteristics of emerging countries’ political environments are well known in the international business literature. This refers to markets that present political instability, reflected in higher degrees of uncertainty, corruption of public officials, volatility in stock markets, changes of power, and unpredictable market regulations. Such institutional aspects related to political environments reduce firm competitiveness and create distortions in markets, which hinders the implementation of products, brands, and business models (Galang, 2012; Lau, Demir, & Bilgin, 2013; Magnusson et al., 2012).

However, firms from emerging markets have certain organizational capabilities that mean they can operate in unstable political environments. This feature of the home market may be favorable in target markets with similar characteristics due to reduced institutional differences in the political environment, making the target market familiar (Cuervo-Cazurra, 2006; Cuervo-Cazurra & Genc, 2008; Oliver & Holzinger, 2008; Perez-Batres & Eden, 2008). Circumventing this adverse institutional factor—a characteristic of emerging markets—value is generated by firms that engage in relationships with governments and political groups (Freeman & Sandwell, 2008; Sheth, 2011).

Faced with these issues, dealing with political instability is not a distant prospect for franchise chains in emerging countries and can be capitalized on as a firm capability through relationships with the government. Hence:

**Hypothesis 3:** Emerging countries with lower levels of political stability are associated with greater commitment by franchise chains from emerging markets.

3.4 | Corruption

Regarding corruption, emerging markets have a completely different environment to that of developed markets (Getz & Volkema, 2001). There are recurring difficulties encountered by many firms to know how to behave in markets demanding kickbacks when doing business. This is not a common ability for firms from developed countries where such practices are socially condemned (Rodriguez, Siegel, Hillman, & Eden, 2006). Consequently, those markets with a high acceptance of corruption face many barriers when attracting international investment, particularly due to the increased risks and uncertainties of the political environment and conducting business (Galang, 2012). Moreover, institutional weaknesses caused by corruption contribute to increased transaction costs, reducing business results and negatively exposing firm governance practices (Djankov, McLiesh, & Shleifer, 2007; La Porta, Lopez-de-Silanes, Schleifer, & Vishny, 2000; Williamson, 1991).

On the other hand, it is clear that secondary markets for firms have attracted investment in recent decades, such as China, Brazil, and India. These markets have economic potential that is recognized by firms of different nationalities. However, these are markets with a corruption imperative that has attracted the attention of scholars interested in understanding these social relations for business success (Blackburn & Forgues-Puccio, 2009). Due to bureaucratic imperatives and the lack of definition of procedures in emerging markets,
kickbacks become an alternative adopted by firms to streamline and facilitate business. Corrupt practices aim to facilitate the approval processes involving government permits and licenses, known as “against the rule.” Moreover, the distortion of edicts and regulations benefits certain firms in public procurement, also known as “against the rule.” Such characteristics of corruption involve low-ranking civil servants as well as senior politicians (Getz & Volkema, 2001; Lau et al., 2013; Pacini, Swingen, & Rogers, 2002).

It is not surprising that emerging-market franchise chains seek markets with similar characteristics to their own domestic realities with regard to corruption acceptance, given the habituality of this commercial practice in overcoming barriers to their commercial activities (Cuervo-Cazurra, 2006; Cuervo-Cazurra & Genc, 2008; Ghemawat & Khanna, 1998). Following these prerogatives, we present the next hypothesis:

**Hypothesis 4:** Emerging countries with higher levels of corruption acceptance are associated with greater commitment by franchise chains from emerging markets.

### 3.5 Market efficiency

Various measures such as price controls, taxes, and trade tariffs are recognized as affecting the degree of market efficiency. Such factors will interfere with the activity of entrepreneurs, with a clear recognition that these aspects influence the competitiveness of enterprises, reducing both financial returns and generating smaller increases in new business creation (Herrera-Echeverri et al., 2014; Klapper et al., 2006; Parker, 2004). For example, governments create incentives by reducing bureaucracy related to starting businesses and reducing tariffs, leading to greater efficiency and enterprise prosperity (Aidis et al., 2012).

However, despite greater commitment by governments to adjust the procedures for business creation and empowerment in developing countries (Herrera-Echeverri et al., 2014), in general, emerging markets have environments with low market efficiency. Factors such as complex tax procedures can become costly to businesses and affect their survival (McMullen, Bagby, & Palich, 2008), especially those that affect smaller businesses, as they have a lack of staff specialized in operations with greater commercial complexity (Sobel, Clark, & Lee, 2007). These enterprises have difficulties in benefiting from tax subsidies and proportionately suffer more from bureaucratic costs than large firms (McMullen et al., 2008).

Faced with these difficulties, emerging-market franchises can take advantage of countries that are similar to their own because they have the ability to operate in low-efficiency market environments. This is not true for chains from developed countries, where such features are inhibitors to investment and commitment (Alon, 2006; Aliouche & Schlentrich, 2009), leading to the following hypothesis:

**Hypothesis 5:** Emerging countries with lower levels of market efficiency are associated with greater commitment by franchise chains from emerging markets.

### 3.6 Moderation effect

In addition to the impact of institutional environments on franchises’ international commitment, one factor is extremely important to moderate this relationship, namely, the size of the franchise chain. Larger chains have greater capability to impose themselves in markets (Kacker, Dant, Emerson, & Coughlan, 2016). Their ability to operate on a larger scale leads to reducing agency costs of monitoring and control activities. This enhances the maintenance and increase of units (Kacker et al., 2016; Michael & Combs, 2008). Conversely, smaller chains have greater difficulties in international operations. Restrictions related to economies of scale, and a lack of technical staff for market research, hinder positioning and success for smaller chains abroad (Shamsie, Phelps, & Kuperman, 2004). In another reality, larger firms have better technical staff and a larger structure for the maintenance of foreign operations (Chung, Chen, & Hsieh, 2007).

Thus, considering the risk involved in international operations, size and scale have some interplay with the selection of countries in which to invest. While acknowledging the institutional weaknesses of developing countries with greater political and legal risks, large firms make large investments in their scales of production (Pak & Park, 2005). This occurs as well with firms originating from emerging countries. For example, in an empirical study with Turkish firms and their destination countries, factors such as political constraints, level of international knowledge, and firm size proved to be essential variables when choosing international markets (Demirbag, Tatoglu, & Glaister, 2010).

Because of these findings, it is expected that larger franchises not only have greater international commitment but also are positively associated with the institutional aspects mentioned above. Therefore:

**Hypothesis 6:** For franchise chains originating from emerging markets, chain size moderates the relationship between institutional aspects and international franchise commitment in destination countries.

### 4 METHODOLOGY

For this research, Brazil was chosen as the emerging country of origin. Most Brazilian franchise internationalization is to destinations in Latin America (Melo et al., 2015)—other emerging countries are Chile, Mexico, Argentina, and Peru. Thus, as our goal is to study internationalization from emerging countries that are destined to the same group, we chose to investigate the internationalization of Brazilian franchises in Latin America. In the first quarter of 2014, the confirmation of Brazilian chains abroad was done through request to the Brazilian Franchising Association (BFA). A list of Brazilian franchise chains with operations in 18 Latin American countries included 119 operating units in the year 2013. Table 1 presents the countries of operation and the number of units in these markets.

### 4.1 Measures and operation

The dependent variable of this research is a composed index of the commitment level of Brazilian franchise chains abroad. This index
### TABLE 1  Operating markets

<table>
<thead>
<tr>
<th>Destination market</th>
<th>Operation units</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>11</td>
<td>9.2</td>
</tr>
<tr>
<td>Barbados</td>
<td>1</td>
<td>0.8</td>
</tr>
<tr>
<td>Bolivia</td>
<td>10</td>
<td>8.4</td>
</tr>
<tr>
<td>Chile</td>
<td>11</td>
<td>9.2</td>
</tr>
<tr>
<td>Colombia</td>
<td>10</td>
<td>8.4</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>6</td>
<td>5.0</td>
</tr>
<tr>
<td>Cuba</td>
<td>1</td>
<td>0.8</td>
</tr>
<tr>
<td>El Salvador</td>
<td>1</td>
<td>0.8</td>
</tr>
<tr>
<td>Ecuador</td>
<td>2</td>
<td>1.7</td>
</tr>
<tr>
<td>Guadeloupe</td>
<td>1</td>
<td>0.8</td>
</tr>
<tr>
<td>Guatemala</td>
<td>2</td>
<td>1.7</td>
</tr>
<tr>
<td>Mexico</td>
<td>10</td>
<td>8.4</td>
</tr>
<tr>
<td>Panama</td>
<td>5</td>
<td>4.2</td>
</tr>
<tr>
<td>Paraguay</td>
<td>24</td>
<td>20.2</td>
</tr>
<tr>
<td>Peru</td>
<td>6</td>
<td>5.0</td>
</tr>
<tr>
<td>Dominican Rep.</td>
<td>2</td>
<td>1.7</td>
</tr>
<tr>
<td>Uruguay</td>
<td>8</td>
<td>6.7</td>
</tr>
<tr>
<td>Venezuela</td>
<td>8</td>
<td>6.7</td>
</tr>
<tr>
<td>Total</td>
<td>119</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Source: Prepared by the authors.

...consists of the number of units in each country over the total units of the chain. The number of units abroad in each country analyzed were considered, which was collected in the Official Franchise Guide (Associação Brasileira de Franchising, 2014) published by the BFA. The number of units abroad is an indicator that is capable of designating the geographic scope of internationalized firms. Within this scope, both the number of units abroad and the number of countries with operations were considered in line with previous research (Ietto-Gillies, 2001; Ramaswamy, Kroeck, & Renforth, 1996; Sullivan, 1994; Tallman, 1996).

Independent variables were built using international indicators in order to analyze the institutional environment of the countries with operations of internationalized Brazilian franchise chains. For this, public data from international organizations that report on the ease of doing business, level of corruption, political risk, and legal regulations were used (World Bank—Doing Business, Transparency International, World Economic Forum, and Heritage Foundation). The data referring to the secondary bases refer to the year 2013 and the editions of these publications correspond to the following year (i.e., 2014).

Institutional aspects are based on previous studies that report on the interference and relevance of these elements in franchise chains’ internationalization process (Alouche & Schlientrich, 2009, 2011; Baena, 2012; Baena & Cerviño, 2014; Grünhagen et al., 2010; Hoffman et al., 2016; Melo et al., 2015). The following constructs were used: (a) cost of enforcing contracts (Aidis et al., 2008, 2012; Henrekson, 2007; Herrera-Echeverri et al., 2014; Hodler, 2009; Parker, 2007; Svensson, 1998; Themozhi & Narayanan, 2016); (b) business freedom; (c) goods market efficiency (Herrera-Echeverri et al., 2014; Klapper et al., 2006; Van Stel et al., 2007; McMullen et al., 2008); (d) political stability and the absence of violence; and (e) control of country corruption (Cuervo-Cazurra, 2006; Galang, 2012; Lau et al., 2013; Perez-Batres & Eden, 2008; Oliver & Holzinger, 2008). Table 2 lists the variables used in this research.

The moderating variable is franchising chain size, which represents the total number of units (independent of being abroad). This variable demonstrates resource accumulation and franchise chain structure (Elango, 2007), which might influence the propensity to franchise (Alon, 2001). Thus, size is an important variable to be considered in understanding the decision to internationalize existing franchising operations (Aydin & Kacker, 1990). This variable was found in the Official Franchise Guide (Associação Brasileira de Franchising, 2014) published by the BFA.

The control variables included are (a) industry segment, (b) GDP per capita, and (c) country quality of infrastructure. The industry segment was grouped into two categories: service firms and retailers of products and food. Previous studies have shown that the industry has a significant effect on the ability of firms to transfer knowledge in international markets through contractual mechanisms such as the franchise system (Buckley & Casson, 2016; Shane, 1998, 2001). In addition, the industry segment’s characteristics might influence the preferences of entrepreneurs for different organizational structures (Martin & Justis, 1993), which may represent differences in business models of internationalizing firms (Alon & McKee, 1999; Elango, 2007). This variable was found in the Official Franchise Guide (Associação Brasileira de Franchising, 2014) published by the BFA.

The other control is the gross domestic product (GDP) per capita. This variable was found in the Heritage Foundation database. GDP per capita was used as a control variable because this dimension is often present in studies on institutional environment, as it represents the economic power of the population by the multinationals (Berry et al., 2010; Das & Banik, 2015) and franchise chains (Baena, 2015; Hoffman et al., 2016).

The last control is the quality of infrastructure variable. This dimension has been verified in other studies that deal with its interference in the institutional environment due to the capacity of companies to access technological structure, logistical access, and other aspects for the multinationals (Dumludag, 2009; Hoskisson, Wright, Filatotchev, & Peng, 2013; Rothenberg, Kotha, & Steensma, 2006) and franchise chains (Hoffman et al., 2016). This variable also was found in the Heritage Foundation database.

For the operationalization of the statistical tests, in addition to compliance with the mean, standard deviation, and correlation, we chose a multiple linear regression model, as there is only one dependent variable. In Model 1, we present the control variables and in Model 2 we add the independent variables and moderation size.

### 5 RESULTS AND DISCUSSION

Table 3 presents means, standard deviations, and correlations. On average, the sampled franchise chains have 311 units, but there is great variance. For example, there are cases of franchises with less than 10 franchise units and others with more than 800. Moreover, the medium number of units abroad is four although some franchises have more than 10 units abroad. According to Table 3, there
are correlations between the independent and control variables. Note that the correlation coefficients are lower than 0.50, except for the correlation between corruption × political stability, and business freedom × market efficiency. However, when checking the variance inflation factor (VIF) in the data analysis models, none of the variables presented a VIF score greater than 10; thus, the

### TABLE 2 Variables description

<table>
<thead>
<tr>
<th>Variables</th>
<th>Description/Measurement</th>
<th>Measure</th>
<th>Source</th>
<th>Ed.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Dependent variable</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Foreign commitment</td>
<td>Number of units in each country over the total units of the chain based on a composite index</td>
<td>%</td>
<td>Brazilian Franchising Association</td>
<td>2014</td>
</tr>
<tr>
<td><strong>Independent variables</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of contracts</td>
<td>It measures the time and cost for resolving a commercial dispute through a local first-instance court, and the quality of judicial processes index, evaluating whether each economy has adopted a series of good practices that promote quality and efficiency in the court system (in % of claims, inverse). Doing Business named as &quot;Enforcing Contracts in % of Claims.&quot;</td>
<td>% (inverse)</td>
<td>Doing Business</td>
<td>2014</td>
</tr>
<tr>
<td>Business freedom</td>
<td>An individual’s right to establish and run an enterprise without undue interference from the state. Burdensome and redundant regulations are the most common barriers to the free conduct of entrepreneurial activity. By increasing the costs of production, regulations can make it difficult for entrepreneurs to succeed in the marketplace (0–10). Heritage Foundation named as &quot;Business Freedom.&quot;</td>
<td>0–100</td>
<td>Heritage Foundation</td>
<td>2014</td>
</tr>
<tr>
<td>Political stability</td>
<td>Measures the perception of the likelihood of political instability and politically motivated violence (0–100). World Bank/Worldwide Governance Indicators (WGI) named as &quot;Political Stability and Absence of Violence/Terrorism.&quot;</td>
<td>0–100</td>
<td>World Economic Forum</td>
<td>2014</td>
</tr>
<tr>
<td>Corruption*</td>
<td>Captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as &quot;capture&quot; of the state by elites and private interests (0–10 inverse). World Bank/Worldwide Governance Indicators (WGI) named as &quot;Control of Corruption.&quot;</td>
<td>0–10 (inverse)</td>
<td>Transparency International</td>
<td>2014</td>
</tr>
<tr>
<td>Market efficiency</td>
<td>This composite index (0–10) is derived from the following indicators: (a) intensity of local competition; (b) extent of market dominance; (c) effectiveness of antimonopoly policy; (d) extent and effect of taxation; (e) total tax rate; (f) number of procedures required to start a business; (g) time required to start a business; (h) agricultural policy costs; (i) prevalence of trade barriers; (j) trade tariffs (k) prevalence of foreign ownership; (l) business impact of rules on foreign direct investment; (m) burden of customs procedures; (n) degree of customer orientation; and (o) buyer sophistication. World Economic Forum named as &quot;Goods Market Efficiency.&quot;</td>
<td>0–10</td>
<td>World Economic Forum</td>
<td>2014</td>
</tr>
<tr>
<td><strong>Moderate variable</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chain size</td>
<td>Total number of franchise chain units</td>
<td>#</td>
<td>Brazilian Franchising Association</td>
<td>2014</td>
</tr>
<tr>
<td><strong>Control variables</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry segment</td>
<td>Segment of operation (Service =1, otherwise =0)</td>
<td>1 or 0</td>
<td>Brazilian Franchising Association</td>
<td>2014</td>
</tr>
<tr>
<td>GDP per capita</td>
<td>GDP per capita</td>
<td>#</td>
<td>Heritage Foundation</td>
<td>2014</td>
</tr>
<tr>
<td>Quality of infrastructure</td>
<td>Transport and communications infrastructure network</td>
<td>0–100</td>
<td>World Economic Forum</td>
<td>2014</td>
</tr>
</tbody>
</table>

*a Corruption variable is an inverse indicator. This means that the higher the indicator, the less corrupted the target country.

### TABLE 3 Average, standard deviation, and correlation matrix

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>SD</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Foreign commitment</td>
<td>4.11</td>
<td>10.94</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Cost of contracts</td>
<td>0.21</td>
<td>0.71</td>
<td>−0.15</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Business freedom</td>
<td>−0.34</td>
<td>0.88</td>
<td>0.03</td>
<td>0.40**</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Political stability</td>
<td>−0.54</td>
<td>0.83</td>
<td>0.10</td>
<td>−0.40**</td>
<td>0.04</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Corruption</td>
<td>−0.42</td>
<td>0.81</td>
<td>0.01</td>
<td>−0.30**</td>
<td>0.42**</td>
<td>0.74**</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Market efficiency</td>
<td>−0.67</td>
<td>1.39</td>
<td>−0.14</td>
<td>0.28**</td>
<td>0.68**</td>
<td>0.16</td>
<td>0.40**</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>7. Chain size</td>
<td>311</td>
<td>492</td>
<td>0.16</td>
<td>0.02</td>
<td>−0.09</td>
<td>−0.09</td>
<td>−0.11</td>
<td>−0.07</td>
<td>1</td>
</tr>
</tbody>
</table>

Note: **p < .01; *p < .05. Source: Authors.
alleged possibility of multicollinearity associations was not present (Hair, Black, Babin, & Anderson, 2010).

Table 4 presents the multiple linear regression models that test the hypotheses. In Model 1, we present the control variables and in Model 2 we include independent variables and the moderating variable franchiser chain size. Model 1 with control variables (quality of infrastructure, industry, and GDP per capita), shows that only GDP per capita has significance \( p < 0.01 \) to explain the international commitment. Industry and infrastructure do not show a significant association. This means that the GDP per capita of the host country is an attractive factor to franchising international commitment.

In Model 2 (full model with control with independent variables and moderating variable–chain size), the result shows that lower contract costs are significantly related to greater franchise chain commitment \( p < 0.05 \). This implies that Brazilian franchise chains are more attracted to markets with lower contract execution costs. As the relationships in franchise chains are based on contractual issues, the efficient contract implementation reduces agency costs for the parties. Institutional environments with weak laws and high contract execution costs make franchisors more vulnerable. In this situation, an institutional environment with lower contract enforcement costs is preferable, especially because it is a common procedure for franchise chains. This hypothesis about the legal institutional environment is aligned with a prevailing theory related to franchise chains’ commitment to legal security in foreign markets (Aidt, 2009; Aidis et al., 2008; Harper, 2003; Henrekson, 2007; Herrera-Echeverri et al., 2014; Hodler, 2009). Hence, the findings are in support of Hypothesis 1.

In relation to business facility issues, the results show a positive and significant relationship between business freedom and chain commitment \( p < 0.01 \). This implies that Brazilian franchise chains are more attracted to markets that are open to business. It is understood from these results that the lack of quality regulation is a barrier to the operation of franchises in similar emerging markets. In this situation, one must consider the particular characteristic of the constitution of franchise chains in which there is the function of the local entrepreneur, in this case, the franchisee. An institutional environment with openness and greater ease in operational procedures and processes in business are thus preferable. In short, even when emerging markets are the destination, the franchise chains consider international facilitators of entrepreneurship markets as a maxim (Belasen & Hafer, 2013; Klapper et al., 2006; Nikolaev et al., 2013; Parker, 2007). This result supports Hypothesis 2.

The results do not support Hypothesis 3. Model 2 shows that Brazilian franchise chains are not more attracted to countries with greater political stability or instability \( p < 0.05 \). Even though these franchises are used to dealing with unstable political environments in their home markets, in international operations they do not tend to prioritize political environments according to instability or stability.

On the other hand, the association of Brazilian franchise chains with host markets that have a greater acceptance of corruption \( p < 0.05 \) is indicated in Model 1. Such a sign of committing to markets that accept corruption shows that they have capabilities to deal with the practice of corruption, which is different from dealing with political instability. That is, franchises create nonlocal capability related to doing business in more corrupt environments. This shows a capability emanating from a disadvantage that can be exploited as a nonlocal capability in other emerging markets lenient with corruption. For example, there are two retailing chains that had more international operation in countries with a greater acceptance of corruption than other markets. In the footwear industry, Arzzo opened the first international store in Venezuela, which is considered a market with high risk and a high level of corruption. This retailing experience led to Arzzo’s having 77% of their international stores located in Venezuela, Bolivia, and Paraguay. As another example, Hering is considered the largest manufacturer and marketer of clothing for men, women, and children in Brazil (Gehrke, Lins, & Borba, 2017). Hering also franchises its retail stores not only in Brazil but throughout Latin America. Most of Hering’s international stores (63%) concentrate in Bolivia, Paraguay, and Venezuela. This result gives support to Hypothesis 4.

Finally, the results show that franchises from emerging countries are associated marginally \( p < 0.10 \) with an increased international commitment to less efficient markets. This is interesting because it contradicts the common sense of being attracted to more efficient markets that could be improvers of entrepreneurial activity (Herrera-Echeverri et al., 2014; Klapper et al., 2006; Parker, 2004). At the same time, they show that in fact, the local capability of operating in business-adverse markets can be capitalized on by franchises and exploited as a nonlocal capability in other emerging markets. For example, Truss Cosmetics, a retailer of professional cosmetic

### Table 4

<table>
<thead>
<tr>
<th>Variables</th>
<th>Model 1</th>
<th>Model 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Control variables</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry segment</td>
<td>-0.099 (-1.080)</td>
<td>– –</td>
</tr>
<tr>
<td>GDP per capita</td>
<td>0.293 (2.521**)</td>
<td>0.374 (2.736**)</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>-0.097 (-0.831)</td>
<td>– –</td>
</tr>
<tr>
<td>Independent variables</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of contracts</td>
<td>– –</td>
<td>-0.492 (-3.274**)</td>
</tr>
<tr>
<td>Business freedom</td>
<td>– –</td>
<td>0.394 (2.538**)</td>
</tr>
<tr>
<td>Political stability</td>
<td>– –</td>
<td>0.043 (0.213)</td>
</tr>
<tr>
<td>Corruption</td>
<td>– –</td>
<td>-0.442 (-2.405**)</td>
</tr>
<tr>
<td>Market efficiency</td>
<td>– –</td>
<td>-0.304 (-1.878)</td>
</tr>
<tr>
<td>Moderations</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chain size</td>
<td>– –</td>
<td>0.460 (3.485**)</td>
</tr>
<tr>
<td>Cost of contracts × Chain size</td>
<td>– –</td>
<td>-0.701 (-2.813**)</td>
</tr>
<tr>
<td>Business freedom × Chain size</td>
<td>– –</td>
<td>0.551 (2.913**)</td>
</tr>
<tr>
<td>Political stability × Chain size</td>
<td>– –</td>
<td>0.134 (0.480)</td>
</tr>
<tr>
<td>Corruption × Chain size</td>
<td>– –</td>
<td>-0.163 (-0.597)</td>
</tr>
<tr>
<td>Market efficiency × Chain size</td>
<td>– –</td>
<td>-0.900 (-3.357**)</td>
</tr>
<tr>
<td>( R^2 )</td>
<td>0.070</td>
<td>0.278</td>
</tr>
<tr>
<td>Adjusted ( R^2 )</td>
<td>0.045</td>
<td>0.194</td>
</tr>
<tr>
<td>F statistics</td>
<td>2.814</td>
<td>3.329</td>
</tr>
<tr>
<td>Model significance</td>
<td>0.042</td>
<td>0.000</td>
</tr>
</tbody>
</table>

Notes: \( t \) values in parentheses; \( **p < .01; *p < .05; \) \( p < .10 \).
products for hairdressers, concentrates its internationalization in less efficient Latin American countries such as Ecuador and Venezuela. The same pattern is observed for Pet Cursos, a franchise chain in the education and training sector that operates internationally only in Ecuador. This finding gives marginal support to Hypothesis 5.

In short, the results show that franchises can turn disadvantages into nonlocal capabilities for institutional aspects related to corruption and market efficiency (Cuervo-Cazurra & Genc, 2008). However, the disadvantage of operating in an unstable political environment cannot be turned into a nonlocal capacity. On the contrary, franchises coming from emerging markets favor stable political institutional environments, with efficient contract enforcement and quality regulations that enable economic freedom.

Even in Model 2, the results show that franchise chains with a larger number of units also have an increased international commitment in Latin American countries ($p < 0.05$). Moreover, size is a moderating factor for some institutional aspects. Model 2 inserts size moderation. As noted, the association of the institutional environment with international commitment is tempered by franchise size. Larger franchises continue to have a preference for institutional environments with greater contract compliance ($p < 0.01$) and business freedom ($p < 0.01$); however, the results show that political stability has no association with the commitment of larger chains. Moreover, when we analyzed factors considered unfavorable that can attract franchise investment and commitment, only market inefficiency was significant ($p < 0.01$) for the larger franchise chains. Corruption acceptance also does not present a significant association.

Figure 2 shows the moderation power of size for contracts, business freedom, and market inefficiency; thus, the results partially confirm Hypothesis 6 where size moderates these variables. Chains with more units have stronger engagement in international operations when institutional factors related to contracts, business freedom, and market efficiency are present. This is in line with theories that argue that larger firms have greater facility in international operations (Chung et al., 2007; Kacker et al., 2016; Michael & Combs, 2008; Shamsie et al., 2004).

6 | CONCLUSION

This article shows that the international commitment of emerging-market franchises in other emerging countries is guided by contract compliance and business freedom. In turn, the franchises do not see high levels of corruption and inefficiencies in doing business as unacceptable obstacles of such environments. The results, on the one hand, constitute a reservation to the current propositions of disadvantage as an advantage for the formation of nonlocal capability and, on the other hand, confirm that the franchises from emerging countries can use disadvantages in their favor as nonlocal capabilities that can be exploited in other emerging markets. In short, the main contribution lies in the partial exception of the arguments of Cuervo-Cazurra and Genc (2008), in which emerging market multinationals (MNEs) are more prevalent in less developed countries compared
with traditional MNEs—evidence of the institutional capability that MNEs possess to turn institutional into their competitive advantage.

For franchises, not all disadvantages may be considered as triggers for building nonlocal capabilities. Contractual issues and regulation cannot follow this logic, which is supported in our results. As for the other aspects of institutional environments, the results show that firms originating from emerging markets can potentially capitalize on the development of nonlocal capabilities that enable them to function in destinations that have low efficiency and a high level of corruption acceptance. However, these chains do not see the capability of operating in unstable political environment as something to be exploited in other emerging markets.

This result supports other studies that investigate the interference of corruption experienced by companies in emerging markets (Cuervo-Cazurra, 2006; Cintra, Cassol, Ribeiro, & Carvalho, 2017; Ghemawat & Khanna, 1998; Kaymak & Bektas, 2015), demonstrating that corruption is not necessarily an inhibitory institutional feature for the operation of Brazilian franchise chains in relation to other emerging markets and least developed countries in Latin America.

A second contribution is related to studies with an institutional perspective (Hoffman et al., 2016; Jell-Ojobor & Windsperger, 2014; Merrilees, 2014) on emerging-market franchise chains’ internationalization (Alon, 2006; Castrogiovanni & Vozikis, 2000; Dant & Grünhagen, 2014; Grünhagen et al., 2010; Merrilees, 2014; Hoffman & Preble, 2004; Welsh et al., 2006). First, investigating institutional aspects defies common sense related to the attractiveness of foreign markets being based solely on the size of population and income (Gouvea, 2004; Gouvea et al., 2016; Narayanan & Fahey, 2005). Second, as pointed out, little is known about the international movement of these franchises in relation to aspects of the institutional environment and it seems important to analyze the results. This is why the results show that existing knowledge can be extended when we see similar behavior in relation to certain aspects, such as contracts, regulation, and politics. However, it takes some relativization given the inversion of values reported for the acceptance of corruption and market inefficiency.

In turn, the contribution to management relates the complex picture of environmental characteristics to be considered by franchise chains in emerging countries. Replicas of their home environment can become a limit to international success, with a fine adjustment of these operations being required in order to prioritize certain institutional characteristics.

This research is limited to choosing only one emerging country. Given the peculiarities of the Brazilian market, one can imagine that perhaps these variables have different characteristics to other franchise chains in emerging countries. It is also limited by the selection of some environmental characteristics (corruption, business freedom, political stability, contract enforcement, and chain size). A research limitation involved the analysis of the year of entry of the franchise chain in the country and its respective institutional environment in this period. We believe that this analysis could enrich discussions about the franchisor's decision making related to the institutional environment regarding entry into the country. This would broaden the current discussion established in the presence of the franchise chain in a given country and its institutional environment.

We suggest that future studies deepen this analysis by selecting more variables and analyzing other emerging other markets, in order to ascertain the determinant characteristics for these emerging chains for different countries or the selection of developed markets. Thus, determining which institutional characteristics are crucial for these franchises is proposed as well as understanding common characteristics and peculiarities of chains with different origins.

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**REFERENCES**


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