

## Russia – an open or closed door for franchises?

by Anatoli Naoumov

Canadian franchises are increasingly looking abroad for chances of future expansion. In some cases, they may believe that they have saturated the market here, or that their offering will have particular resonance in another market.

Russia is an often-overlooked possibility for international growth, but one that is showing new promise. To some extent, this market is particularly open to Canadians, who are seen as less aggressive and pushy than Americans, and more capable of adapting to a different environment.

While some Westerners see Russia as an uncontrolled wilderness of organized crime, extortionate taxes and economic chaos, the fact is that these perceptions are mostly outdated. These stories are only three or four years ago in terms of the calendar, but they are a whole era away in business management terms. Russia's current government values stability and is working hard to promote it. Current economic forecasts, from many sources, indicate that Russian incomes will triple, in real terms, over the next decade. Although this may be an overestimation, real income growth is visible already now. This spells "opportunity" for Canadian businesses, including foodservice and hospitality franchises.

However, it is equally unwise to hold the view that Russia is a land of boundless optimism, where anything "Western" will be snatched up by eager Russian hands. If this was ever true, those times are also gone. Low-cost, high-quality Asian goods have long been available in Russian stores, for example, giving North American and Western European goods serious price competition. Many members of the growing middle class take vacation trips to Western Europe once a year, so are unlikely to be dazzled by your offering simply because it has that Western cachet.

Between these two extreme views we have the reality of Russia today – where the business practices are different from those of the West and where the unwary can still learn extremely expensive lessons, but also a place where hard work and sound business practice can pay off.

One important thing to understand about Russia is that it is rapidly evolving into two solitudes. There is the cosmopolitan, dynamic near-Western world of Moscow and St. Petersburg, where some stores offer more variety than do similar stores in Canada. This world contrasts greatly with the rest of the country, where the economy is less advanced and the people have much lower incomes. Because Moscow and St. Petersburg offer the greatest opportunities, we will concentrate on those cities in this article.

### ***What does the Russian market value?***

Before entering the Russian market, you must research your product offering to be sure that it is competitive and possesses a clear value to local customers.

Russians do not generally lack for food, but they do hunger for quality food provided consistently. Franchises with well-considered recipes and procedures can be in an excellent position to offer what the Russian public wants.

Russians do not go to a restaurant just for food – they want an experience and entertainment. Themed restaurants are very popular now.

## **Success factors**

In Russia there are many highly educated people who can help you navigate the intricacies of the market. Many have received a good business education, including MBA degrees or similar. This means you should hire qualified people and support them – and they will support you.

A big success factor, regarding your Russian employees, is hands-on management. Do not rely on phone calls and e-mails; being personally present much of the time is important. Every visit by a Western-based employee should be an opportunity to reinforce your corporate culture.

Keeping close control is important in dealing with the issue of employee theft and fraud. Russians are not prone to this any more than anyone else, but they will watch carefully to see whether you are really “managing” your company or if you are losing control. If you do not care what happens to it, why should anyone else?

Russians are very sensitive to honesty in business, particularly in areas such as transparent business procedures, and equality in promotion and compensation. One reason for the sensitivity is that for decades they had a government that said one thing and did something quite different. Business owners who do not live up to their own declared standards should not be surprised if the next stocktaking turns up significant shortages. Russia is no different from any other country in this respect.

In other areas as well, your people are key to your success. Business in Russia is not so much about money as it is about people. Build your business on your employees, make them proud of working for your business and they will help make it famous.

One of your most important staff choices is your head of Accounting. Part of this is because the taxation picture in Russia is ever-changing and the regulations are often subject to interpretation. You need a professional accountant on your side who understands the tax code, and equally important who is able to know current practices in developing good relations with the local tax authorities, whose interpretations of the code influence the tax you are assessed.

In managing your operation, you may be tempted to rely on Canadian staff on secondment. There are several disadvantages to this approach. One is that you need management in place for the long haul, and few Westerners will want to stay for the time period required. Another is that if you provide higher pay and benefits to Western employees, this will soon cause a rift with Russians who believe that they are equally or better qualified and should be paid accordingly.

Therefore, it is probably best to choose locals who are likely management material, provide training and acculturation along with your Western management trainees, and then give them the authority they need to get the job done in Russia.

## ***What are the special challenges of the Russian market?***

In the case of foodservice, keeping quality standards and profitability margins both high is perhaps the biggest challenge.

For ideas on how to do this, consider a tale of three Western operators, all established in the Russian market. All enjoyed high margins and wild demand – before the currency crash of 1998, when the ruble dropped in value from six to the US dollar to 25 to the dollar in a matter of weeks.

McDonald's followed the ruble down and made up for it with creative marketing and careful local sourcing. Now, this company is perceived as a local company, with tremendous customer loyalty and crowded outlets, with lineups at almost any time day or night.

By contrast Carrols (franchisee of Burger King, Taco Cabana and Pollo Tropical) kept US dollar parity pricing and was soon out of the market.

Baskin-Robbins took the middle road and is still in business, but is losing to local competition on price.

It is clear that it is best to consider your market for the long term, and plan your activities from this perspective.

Russia is clearly a land of great potential, given the size of the population and the prospects for growth. However, it is equally clear that success in this market demands careful planning and a willingness to learn.