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BALANCING FRANCHISE GROWTH WITH AID TO SMES

On February 11, the Ministry of Trade issued a new regulation to limit the expansion of international restaurant chains, such as McDonalds, KFC and others. The regulation stipulates that the number of outlets owned and managed by either a franchisor or franchisee cannot exceed 250. However, if the company already operates 250 outlets, and would like to add more outlets above the 250 limits, the new outlets have to be franchised by way of a joint venture with a small or midsized enterprises (SMEs).

The goal of the new regulation on the size of franchise chains is to empower SMEs, promote domestic products and limit franchise control by one entity. This new regulation supplements regulation issued last February on the implementation of franchising. The new regulation only affects food and beverage outlets. The new regulation defines a joint venture arrangement under two categories of investment value. If the investment value is less than Rp 10 billion, the investment by the franchisee should be at least 40%; if it is over Rp 10 billion, the investment by the franchisee must be at least 30%.

The regulation emphasizes the importance of SMEs. The government's intention is clear: it wants to further and support the interest of the SMEs, particularly those outside Jakarta. For that purpose one has to appreciate this positive intention as SMEs are the backbone of the Indonesian economy.

It is obvious that the limitation of 250 outlets would not significantly impact the international chains, as that number is not small. However, a chain can still control additional outlets established through a joint venture with them should they fail to fulfill their requirements. If this happens, the noble intention of this regulation will not be achieved since the franchise will remain in the hands of large enterprises.

Another interesting point to note is that the Indonesian Association of Franchise and License (WALI) claims that the new regulation violates Article 35 of the law on micro, small and midsized enterprises. Briefly, Article 35 states that a large enterprise is prohibited to own or control micro, small and midsized enterprises as its partner in a joint venture. On this issue, WALI plans to file a judicial review against the regulation to the Supreme Court.

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equity control up to 70%. In other words, although the regulation is meant to help SMEs, it still gives control to international chains.

As SMEs may only have a minority stake, they may be only passive investors and not be involved in day-to-day management. This means the SME partner may not gain much know-how in the franchise business. Even though the regulation requires a franchisor to prioritize SMEs, a franchisor has the right to reject

The judicial review and the downside of this regulation notwithstanding, the limitation on food and beverage franchises is a good idea. No party should hold a monopoly on the franchise business in Indonesia. However, the government would need to supervise the implementation of this regulation to ensure that it is effective. Franchisors and franchisees are smart, they may find ways to get around these official rules. The government has to make sure that this will not happen.

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