
FRANCHISING — A PARTNERSHIP MODEL FOR EFFICIENT WATER SERVICES OPERATION AND MAINTENANCE

Authors

Dr. Kevin Wall (Manager: Urban Management and Infrastructure, CSIR Knowledge Services, South Africa)
Jay Bhagwan (Director: Water Use and Waste Management, Water Research Commission, South Africa)
and
Oliver Ive (Managing Director, Amanz'abantu Services, South Africa).

(First author: CSIR Knowledge Services, P O Box 395 Pretoria 0001 South Africa; +27-82-459-3618; kwall@csir.co.za

Second author: Water Research Commission, Private Bag X03 Gezina 0031 South Africa; +27-12-330-0340; jayb@wrc.org.za

Third author: Amanz'abantu Services, PO Box 19442 Tecoma 5214 South Africa; +27-43-726-7217; oliver@aserve.co.za)

*Paper prepared for the Fourth IWA Specialist Conference on the Efficient Use and Management of Urban Water Supply.
Jeju Island, Korea, May 2007.*

Keywords

water and sanitation, water services, franchising, delivery

Abstract

There is a need in South Africa for institutional innovations aimed at increasing the coverage and reliability of water services, and sustaining those services. The paper describes an alternative service delivery institutional concept, viz the franchising of the operation and maintenance of water services, and outlines the need to formulate a franchise model that could be developed and made available to emerging entrepreneurs as the basis of a viable business. The franchise would be in respect of components of the water services value chain that are suitable for small business in that they can be readily systematised.

Introduction

The capacity of many municipalities in South Africa to adequately provide even basic levels of water services to all their citizens is in question. The need for new alternative service provider institutions is apparent.

Both the parastatal regional bulk water supplier Rand Water and the national Department of Water Affairs and Forestry (DWA) have for a number of years considered that the potential for franchising in the water services industry ought to be investigated. For various reasons this has never been done.

Note to conference organisers: while the two figures usefully complement the text of the paper, the paper is probably clear enough without their inclusion. Thus, if space does not permit, they can be omitted.

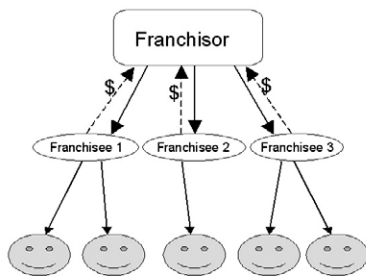
Franchising

Many goods and services are supplied by small-, medium- and micro-enterprises (SMMEs). However starting a small business is never an easy task. Difficulties to be resolved include those of understanding the business method, establishing the need for the product and an image for the product, setting up the business (with attendant capital costs), finding out which regulations apply and then complying with them, and recruiting and training staff.

The barriers to entry for the start-up SMME in any field of enterprise are substantial. If these could be overcome, then many more business opportunities will be enabled, and the probability of business failure will be reduced.

Franchising (more correctly “business format franchising”) is a way of using tried and tested methodology to accelerate the development of a business. The right is granted by a business entity (“the franchisor”), to a smaller entity (“the franchisee”), to use a business method or system. In return, the smaller entity pays fees to the larger. The assistance that the franchisor gives with setting up the franchisee’s business, and the ongoing training and support of the franchisee and quality control of the goods or services, are usually also part of the agreement between them. **Figure 1** — OPTIONAL — here. There is no direct contractual relationship between the franchisor and the customer/end user of the goods or services.

Thus the process of formulating a franchise system firstly correlates and systematises the business, and then the franchisor facilitates the setting up of the business, and supports and disciplines it as a going concern thereafter. For good reason, franchising can be summed up in the slogan: “Being in business for yourself but not by yourself”.



- Under the franchise ‘brand’ franchisees receive business ‘know-how’ from franchisor and provides services / products to customers
- Franchisor monitors quality of product / service to customers
- Customers pay franchisees for products and services and a % is passed back to the franchisor as a royalty payment

Franchising – a business methodology, based on the duplication of success, between two or more separate legal business entities operating under the same brand name.

Figure 1: Franchising overview

Whereas the incentive to start up a small business is the prospect of a quantifiable financial outcome (profits, dividends or surplus), the presence of a successful business model that can be copied is the incentive to follow a franchise route as opposed to following a route without the support of franchising. These, the prospect of profits/dividends/surplus on the one hand, and on the other hand the model that can be copied and the reduced risk to the franchisee thanks to the support of the franchisor, are the twin driving

forces of the franchise concept.

The cardinal elements of the franchise process are thus:

- Identifying a component (or components) of the value chain that is simple enough to systematise
- Discovering best practice
- Systematising the business
- Selecting franchisors and franchisees
- Training
- Preparing operations manuals
- Research and development
- Continuing support, control and discipline of the on-going business.

For-profit franchising of commercial goods and services in South Africa is extensive, generally viable, and growing rapidly, generating retail turnover that (excluding retail petroleum outlets) accounts for of the order of 6.5% of all retail turnover in South Africa. Significant numbers of jobs have been created. There is much evidence that, everything else being equal, franchised businesses have a far lower failure rate than do independent businesses.

The water services investigations

South Africa is one of the few nations in the world where in most urban areas water can safely be drunk directly from a tap.

The parastatal research organisation the Council for Scientific and Industrial Research (CSIR) has estimated that the current replacement cost of the water services infrastructure that is the responsibility of the 170 water services authorities (municipalities or combinations thereof) is at least R 120 billion (“billion” = 1000 million), and that the current replacement cost of the water services infrastructure that is the responsibility of the 15 water boards is of the order of R60 billion. (R 180 billion is of the order of US\$ 25 billion at current exchange rates.) At least a quarter (by current replacement cost) of that infrastructure has been constructed since 1994.

This constitutes an enormous amount of water services infrastructure that is in place and is (or should be) delivering services, and has to be operated and maintained. Furthermore, a stringent timetable has been set for the eradication of the backlogs in provision of basic services. In terms of the timetable, all households will by 2008 have access to a functioning basic water supply, and to a functioning basic sanitation facility by 2010. From this it can be inferred that there will be a steep increase in the amount of water services infrastructure that will have to be operated and maintained.

DWAF has for some time expressed concern as to how well water services infrastructure is (or is not) delivering a service. Every ministerial budget speech of recent years has raised the issue of the cessation of delivery due to failing infrastructure.

The institutions, especially the municipalities, which have the responsibility for operating and managing this

4.3D

infrastructure are for the most part being severely challenged. Current institutional approaches, together with lack of capacity and skills, are in some instances inadequate to support the main aim of the new infrastructure programmes, viz to improve the access of the poor to basic services.

Even in the well-resourced municipalities, although the service may be reliable, efficiencies are sometimes unacceptably low. Water losses, for example, are significant, due largely to a legacy of underfunded maintenance budgets and inadequate maintenance practices, a generic problem in many developed countries, and more so in many developing countries.

Given the changes in the customer base of municipalities, and changes in technology and new service levels, innovative thinking and approaches to water service delivery are required. But even if all the existing institutions were coping with the water services delivery responsibility, there would be good reason to investigate alternative institutional models, on the grounds that it needs to be found out if alternatives:

- could be more cost-effective, and/or
- could allow existing roleplayers to focus on their other responsibilities, and/or
- could offer a range of other advantages (including greater community participation).

Internationally, it has been recognised that there is a need for partnerships between public, private and civil institutions to achieve water services delivery objectives. The variety of partnerships that has been implemented, viz. private sector concessions, Build-Operate-Transfer (BOT), Build-Operate-Train-Transfer (BOTT), etc., has enjoyed mixed success overseas and in South Africa. These have generally been “big business” partnerships for large scale contracts, and generally investment (public or private) in new infrastructure plays a prominent role.

There is an alternative service delivery institutional model that is suited more for the ongoing operation and maintenance of water services systems, and not for investment in new infrastructure — and that is friendly to small business and local economic development. This alternative is the franchising of water services. However there is little experience of this approach anywhere in the world, and no experience in South Africa — although some partnerships have some of the characteristics of the franchise approach.

To address this, the South African Water Research Commission (WRC) initiated a study to explore the subject and concept of franchising, its relevance to the water services sector, and its prospects as an option for water services operations and management.

Neither of the “twin driving forces” of the franchise concept, referred to above, is currently in evidence in the water services sector in South Africa. Furthermore, there are many pitfalls when it comes to implementation even under the most favourable of circumstances.

There is little experience of water services franchising anywhere in the world, and no experience in South Africa, although some existing partnerships have some of the characteristics of the franchise approach. A survey of overseas literature, while conceding that the topic of water services franchising is a very new one, and implementation even at a pilot scale is yet to take place, found that it is considered that water services franchising shows great promise (Roche et al., 2001; Van Ginneken et al., 2003). Especially this is so in respect of water services to small towns and to multi-village schemes.

The need in South Africa for less unemployment, for higher household incomes, and for more entrepreneurs, is unquestionable. It is intolerable that of the order of 40% of those between 15 and 65 have no formal jobs. Furthermore, South Africa ranks low in global entrepreneurship surveys, indicating failure to create a competitive climate in which emerging businesses can grow and thrive. Thus the need for local economic development, and in particular the need for the creation and nurturing of SMMEs, is additional motivation for the investigation of franchising in South Africa as a water services delivery concept in addition to, and complementary to, the current operational models.

While water services SMMEs need by no means be franchisees, it is the franchising of water services that is the subject of the ongoing WRC investigation and the subject of this paper.

The findings

The WRC study (Wall 2005a, Bhagwan et al 2006) found that the franchising concept, if applied to water services delivery, could in favourable circumstances both alleviate problems encountered in and raise the efficiency of water services delivery. At the same time, franchising would have the added advantages of stimulating small business activities.

A key is the incentive, to franchisor and franchisee alike, to improve efficiency.

The study described at a conceptual level how a water services franchise model could be made available to emerging entrepreneurs, and concluded that this could be the basis of a viable business. The franchise would be in respect of a component of the value chain that is suitable for small business because it can be readily systematised. The study indicated opportunities in the water services delivery chain, and recommended that these be further explored.

The study found that the great need for alternative water services provider systems, and for local economic development, is indisputable, and that there is through water services franchising potential to simultaneously:

- more consistently deliver water services to specification;
- improve water services efficiency; and
- promote local economic development, SMME development and (a major objective of the current South African government) the empowerment of Black people who were disadvantaged by the apartheid government that was in office until 1994.

Thus “franchisee” must be added to the list of possible water services provider types in South African water services practice. Figure 2 — OPTIONAL — here

However, franchising would be by no means free of many of the issues that equally affect other water services delivery alternatives. Franchising would be just as dependent on the criteria being in place for sustainable delivery, and just as dependent as current delivery institutions are on any external sources of finance.

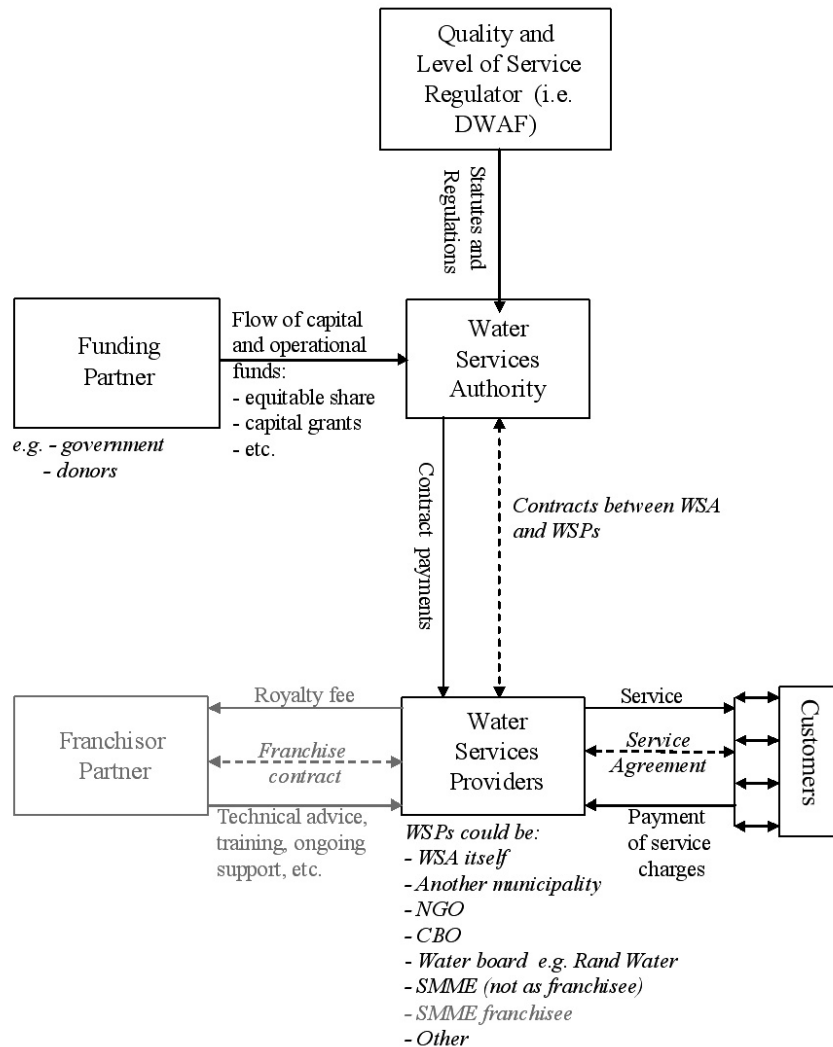


Figure 2: Simplified present relationships with franchising alternative option added(in red)

The WRC study found that it is essential to the success of water services franchising that, inter alia:

- Service to customers meets the specification in the franchise contract with the water services authority
- Suitable franchisors are willing and available
- Local entrepreneurs are willing to take up water services franchise opportunities
- Franchising proves to be a viable business for franchisor and franchisee alike
- Funding partners support water services franchising in just the same way as they support in comparable circumstances water services provision by other institutional means

On the last of these points: Franchising must benefit from the funding streams (e.g. the “Equitable Share Programme”, a major national government welfare funding programme directed at the poorer municipalities) to the water services authority (i.e. municipality) to the same extent as these streams benefit any other type of water services provider.

Franchisee water service providers, dependent for their livelihood on the success of their business, would have a strong incentive to perform, and would also enjoy the benefit of the franchisor’s expert guidance and quality assurance. On this latter point, a franchisor can ensure a professional approach, quality control, and ongoing training, as well as advice and help when needed.

This help from the franchisor would be of particular value in municipalities away from the major urban centres. Few of these municipalities can afford to employ competent qualified staff. Sample surveys of these municipalities’ treatment works, for example, show frequent non-compliance with the performance standards laid down. (DWAF 2005; Snyman et al 2006; Wall 2005b) Significant improvements would soon be seen if the generally under-qualified or under-resourced water services staff in these municipalities could have this ongoing support, mentoring and quality control — or if the municipality could contract this out, entering into agreements with SMMEs who would enjoy the necessary ongoing support, mentoring and quality control.

Given that the costs of the franchisor’s higher levels of specialist expertise are shared by several franchisees, the franchisor could afford to make this expertise available to each of them on an as-needed basis, and could provide other resources normally only available to larger water services providers. This holds significant benefits for municipalities.

Thus there is ample scope for the SMME private sector to assist, and there should be a range of ways in which entrepreneurship in water service provision can be encouraged and supported. If the entrepreneurs were not stand-alone enterprises, but were franchisees, they would enjoy competent franchisor support, and both franchisee and franchisor would be incentivised to make this arrangement work. Many useful pointers can be found in business format franchising franchisee development programmes as well as in engineering infrastructure contractor development programmes, both of which have good track records in South Africa.

The municipal client’s competence to monitor performance and enforce contract compliance is key to it effectively using the SMME sector. However if a municipality is short of management resources, it would be putting these to more efficient use in managing the work of the contractor than in trying to cope with the operational issues itself.

It is not unreasonable that the private sector can be contracted to supply water services, and take the profits that the contracts permit. There should be no ideological barrier to this — and given that there are currently not enough water services providers in South Africa, entrepreneurs should be offered the opportunity to assist. Franchising, being a type of private sector participation, will be challenged in the same way as private sector participation in water services operation generally has been challenged in South Africa — challenged, that is, both politically (e.g. municipal trade union opposition) and institutionally (where procurement legislation puts hurdles in the way).

4.3D

Nevertheless, the argument for franchising as a means to improve efficiency in water services operation and maintenance does not depend on the case for or against the participation of for-profit organisations, and there are already elements of franchising in some of the current activities of non-profit water services organisations in South Africa. For example, a valuable asset to several predominantly rural municipalities currently is the practice of appointing large water services institutions as “support services agents” to support water services providers that are non-governmental organisations (NGOs) and small, local community-based organisations (CBOs). Although this arrangement is not franchising, development of the franchising concept can definitely learn from its experience, and it could also benefit from adoption of some of the characteristics of franchising.

Two organisations, one a parastatal and one from the private sector, that have the expertise and resources to play a franchisor role, have expressed interest in playing such a role, should the opportunities arise. There is little doubt that other capable organisations would be interested were they to see the potential.

A new study

In 2006 the WRC appointed a team led by the CSIR to begin a more in-depth investigation into water services franchising, but stopping short of implementation even at pilot scale. Deliverables will include:

- Review of statutory, procurement, and other issues which could impact on water services franchising, and development of guidelines for regulating franchising
- Identification of elements in the water services delivery chain which offer the greatest scope for franchising
- Development, guided by established principles for franchising of a business (FASA 2005), of franchising models for the areas identified by the research.
- Case study of an element or elements in a hypothetical situation, to see how this would work
- Development of guidelines for setting up water services franchising.

Piloting of the concept might be contemplated after completion of the new study.

The study is also looking into a number of water services institutional arrangements that exhibit some of the characteristics of business format franchising, in order to assess if these concepts might also be valuable alternatives for water services operation and maintenance in South Africa. An example of this is eThekweni Water Services’ newly-begun latrine maintenance project which is not by any means true franchising, but does have influences of franchising, management contracting, and other antecedents. (EThekweni is the metropolitan area that includes Durban.)

At the same time, the research has been formulating a number of proposals that it is hoped will in due course become pilot projects. These proposals can readily be grouped into two types, as follows:

- Proposals that would lead to the establishment of franchisee water services providers, offering a full range of water services
- Proposals that would lead to the establishment of franchisees who would offer selected services under contract to water services providers

In respect of the first, initial discussions have been with DWAF, with a view to structuring a partnership between themselves (providing technical and funding support) and a water services authority (a municipality) that is responsible for areas including small towns and rural villages. The intention is to set up a pilot project in a selected area that would involve the development of a local franchisee as the full-service water services provider for the area. The franchisor could be one of the well-resourced organisations that has already expressed interest in playing this role.

The second type of proposal that is being worked on is somewhat different, and may best be explained by way of describing what at the time of writing are the two most comprehensively formulated of the several promising prospects being worked upon. The first of these relates to plumbing services in an urban area. The second relates to rural schools sanitation.

About two dozen years ago, a young Pretoria plumber who had started out on his own realised that the only way to increase his turnover (and profit) through replication of the prompt service that had become his business' trademark, was to franchise the business. Which he duly did, and the business has grown rapidly ever since. He subsequently added an electrical business, and in due course franchised that also. (It is of note that in this instance the franchisees operate under the franchisor's brand name. Brands are important in competitive retail or service markets, but there is much less (if any) experience of the use of branding in markets where competition is limited or nonexistent. The value of brands, and their appropriateness to water services operation, is an issue that needs to be explored.)

However, all of his custom has been received from the owners of commercial properties and the higher-income residential properties. The current proposal is to extend, to the vast residential townships where the municipality is the property owner, the kind of service that he provides elsewhere. Affordability in these townships is, generally speaking, low, and when a plumbing problem occurs the residents either wait for the municipality to repair it (which could take days, and meantime water is wasted or wastewater backs up, depending on the nature of the problem), or they fix it themselves or get a neighbourhood amateur to do it for them, invariably inadequately. The proposal is to structure a deal with the municipality, whereby the plumber-businessman referred to above selects local residents, sets them up as franchisees, trains them in the technical and business skills, and in all ways acts as franchisor as he does elsewhere in Pretoria.

The municipality would have to subvent the business to make it viable (much as it subvents its own plumbing operations in the townships). However, preliminary estimates suggest that this will cost the municipality less than it is presently spending in the townships, and it will be granted the assurance that the residents will receive a much better service than they presently do.

The second especially promising prospect is a proposed innovative approach to solve a serious sanitation problem in the Eastern Cape. In brief, sanitation facilities at the majority of the rural schools in that province are not up to minimum standards, and few of the schools have management capacity to be able to refurbish or upgrade the facilities, or even to carry out basic operations and maintenance. The proposal of the provincial education department is to appoint SMMEs (it is estimated that around 60 will be needed), under the guidance of one or more managing contractors, to undertake the necessary one-off facilities improvement, and thereafter to operate and maintain the facilities. An alternative proposal, being put to the department, is that once the one-off facilities improvement has been completed, the ongoing operations and

4.3D

maintenance be franchised. In other words that the SMMEs responsible for ongoing operations and maintenance be franchisees, guided by a franchisor (maybe more than one).

A formal proposal has been made to the provincial education department. At the time of writing a decision on this proposal had not yet been made.

Conclusion

Although it is still early days in respect of the development of the concept of franchising for more efficient water services operation and maintenance, its prospects do appear promising.

References

Bhagwan, J, Wall, K, Ive, O, and Duvel, R. (2006). Towards models for franchising in the water services sector. Water Institute of Southern Africa conference, Durban, May 2006.

DWAF. (2005). Water services infrastructure asset management strategy study. Phase 1: status report. The state of water services infrastructure and its management: a desktop strategic study. November 2005. (Consultants CSIR, in association with Matingi and Associates, Makgoleng Projects and Pula Strategic Resource Management.)

Franchise Association of Southern Africa (FASA). (2005). How to franchise your business.

Roche, R, Revels, C, and Amies, M. (2001). Franchising in Small Town Water Supply. The World Bank, Washington DC, February 2001.

Snyman, H, van Niekerk, A M, and Rajasakran, N. (2006). Sustainable wastewater treatment ? what has gone wrong and how do we get back on track? Water Institute of Southern Africa conference, Durban, May 2006.

Van Ginneken, M, Tyler, R, and Tagg, David. (2003). Can the Principles of Franchising be Used to Improve Water Supply and Sanitation Services? — A Preliminary Analysis. Bank Netherlands Water Partnership/World Bank, June 2003.

Wall, K. (2005a). Development of a framework for franchising in the water services sector in South Africa. WRC Report No. KV 161/05. Water Research Commission, Pretoria.

Wall, K. (2005b). Water and wastewater treatment works in South Africa: a study of the compliance and regulatory gap. Poverty reduction through better regulation” conference, Johannesburg, February 2005.