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GEOGRAPHICAL DISTANCE, CULTURAL DIFFERENCES, AND DIGITALIZATION: CRITICAL DETERMINANTS FOR FRANCHISE EXPANSION ON INTERNATIONAL MARKETS

Abstract: *This study examines the impact of geographical distance, cultural differences, and digitalization on the internationalization of Croatian franchise businesses, incorporating a thorough analysis based on the 2022 Global Market Potential Index. Covering 97 countries, the research specifically focuses on 22 European Union nations, which are evaluated for their potential to expand franchising operations. The analysis delves into various dimensions, including market potentials, geographical proximity, and the degree of digitalization, with particular emphasis on access to digital public services.*

Notable findings highlight those countries like Ireland, Germany, Switzerland, and the Netherlands, with their robust market sizes, significant trade volumes, and high economic growth, rank among the top ten on the global index. This underscores the substantial impact of the European market on the franchising internationalization processes, with ten EU countries featuring prominently among the top twenty positions.

The study also discusses the positioning of Germany, Ireland, and Belgium at the top of the list, contrasting with countries such as Bulgaria, Greece, and Latvia, which exhibit lower potential for franchising expansion. The proximity of markets like Serbia, Bosnia and Herzegovina, and North Macedonia is recognized; however, these countries are not extensively analyzed due to their geographical closeness and presumed familiarity to Croatian entrepreneurs, which poses fewer challenges in market expansion decisions.

To facilitate informed decision-making in the internationalization process, this paper extends the analysis to include cultural factors, geographical distances, and the level of digitalization in target markets.

Keywords: *franchise; internationalization; market potential; digitalization; cultural differences*

1. Introduction

In the dynamic context of macroeconomic changes, globalization processes, and the continual pressure for economic growth, entrepreneurs are increasingly required to adapt through business expansion and development. Business expansion is often constrained by limited resources, both internal, such as funding capabilities, and external, including competitive pressures and limited demand in domestic markets. Expanding operations into international markets presents both an opportunity and a challenge to utilize available resources efficiently. Initially, exporting products or direct foreign investment may seem like suitable strategies; however, franchising has proven to be a successful and viable model for distributing products and services (Konigsberg & Rosenstein, 1991).

The franchising is a cooperation model between two independent parties: the franchisor, who provides their brand, ensures a business model, and offers support, and the franchisee, who pays fees and commits to operate according to established standards (Kukec & Petar, 2023). In the franchise business model franchisor grants the franchisee the right to distribute products and services under a franchise agreement. The word franchise comes from the Anglo-French verb *franchir*, meaning "*to free itself*". This means that, unlike direct foreign investments, in this model, another business entity freely, but in accordance with the terms of the franchise agreement, handles distribution in

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a new geographic area. In this scenario, choosing the appropriate location and a suitable franchisee can be crucial for success.

As digitalization advances among entrepreneurs and continues to develop globally, alongside the ongoing trend of globalization, some aspects of risk associated with international business operations in comparison to the pre-digital era significantly decrease. Digitalization facilitates access to customers and information on targeted international markets, also enhances communication, and reduces company costs. On the other hand, digitalization brings with it numerous risks related to the security of communication channels and data, which need to be taken into consideration which is not the subject of this paper.

The diverse cultural differences between countries, varying consumer preferences, and the availability of digital channels, travel, and media have enabled consumers in most countries to recognize and access products and services from abroad. Despite this, selecting a qualified and motivated franchisee remains irreplaceable. The ability to find innovative solutions for adapting systems while adhering to the franchising norms of standardization in the host country becomes a critical characteristic in selecting qualified franchisees. Moreover, the development of a franchising ecosystem, both in the entrepreneur's home country and in the targeted international market, is crucial for the successful internationalization of franchising operations.

This article is a part of the research "Franchizing in Entrepreneurship" (the Kukec & Petar's book is also part of achieved results) so goal of the research is to make business analyses of franchizing and opportunities for entrepreneurs. In this article, the research was conducted using the collection and analysis of publicly available statistical data. As a result, the research is classified as secondary research or desk research.

In the brief overview of the research content, the study involved an examination of the existing literature on the topics of franchising and internationalization, as well as the analysis of available statistical data related to the global market potential. In the research process for this paper, geographical distances were calculated, and a calculation of cultural differences between the observed countries was conducted.

The aim of this research is to develop an index of franchising potential among selected countries from a Croatian perspective. This index considers three key factors: global market potential, cultural and geographical distance, and the degree of digitalization. Also, the purpose of this research is to contribute to the franchising ecosystem in Croatia by providing a deeper understanding of the opportunities for expansion into international markets, based on the conducted studies.

The central research question of this paper is: How do cultural differences and geographical distance between Croatia and selected countries influence the success of Croatian franchise models when expanding into these markets?

This question arises from the need for a better understanding of the factors that affect the internationalization of franchising in Croatia. The research focuses on analyzing how specific factors, such as cultural differences and geographical distance, can impact the adaptation and success of Croatian franchises in international markets.

This paper delves into the impact of geographical distance, cultural differences, and digitalization on the process of internationalizing Croatian franchise businesses, highlighting their implications on strategic decision-making and market expansion strategies. For small and medium-sized entrepreneurs whose choices significantly depend on limited resources, the selection narrows to geographically and culturally closer markets (Stanković, 2020).

2. Franchising

Franchise model enables rapid business expansion with relatively low investment for the franchisor and reduced risk for the franchisee, utilizing an already established and recognizable business concept. The author argues that the franchising model necessitates detailed development, a high level of documentation, standardization, and the establishment of business structures and operational procedures, along with ongoing support for franchisees. In return, a qualified franchisee is required to pay an initial fee and ongoing royalties, which grants them the right to use the franchisor's brand and business model (Kukec, 2019). This arrangement allows the franchisee to operate within a specific geographical area, encouraging rapid expansion and providing entrepreneurs access to a previously proven business concept with reduced/ shared risk.

The prerequisite for creating a franchise system, known as "franchisability," refers to a company's development, credibility, adaptability, and ability to replicate its business model. This includes proven brand, ongoing success, established procedures, the ability to transfer knowledge and operational procedures, and the capability to offer continuous support and training to the franchisee. According to the author, 'franchisability'—the capacity of a business to be franchised—depends on clearly defined standards and a systematized structure to ensure consistency and quality across the franchise network.

The relationship between the franchisor and the franchisee is complex, dynamic, and scalable, bringing with it certain challenges but also significant potential arising from their strategic alliance. Some franchise systems expand only through area or multi-unit development. By working with fewer, larger franchisees, they can streamline management and focus on support, new products, and services. (Seid & Thomas, 2011)

The franchise agreement forms the foundation of the business relationship between two or more parties in franchise operations. In addition to adhering to the agreed-upon terms, the franchisee is also expected to comply with the operational procedures imposed by the franchisor's brand. Therefore, the franchise agreement is crucial for implementing quality control within the franchise system.

The European Code of Ethics for Franchising fundamentally addresses the franchise agreement, outlining the essential minimum requirements that each such contract must include to ensure a win-win relationship between the two partners. (Kukec & Petar, 2023).

The research results reveal that lower performance is not primarily due to poor relationships, between partners but rather to financial difficulties that trigger conflicts (Perrigot, 2020). Franchise systems require ongoing communication, feedback, and collaboration between the franchisor and the franchisee to maintain quality control and address any outstanding issues. (Lafontaine, 1992).

There are various ways in which franchisors oversee the implementation of the contract and adherence to operational procedures and quality standards by franchisees. These can include audits, mystery shopping, customer satisfaction surveys, customer complaint resolution in franchise networks, and monitoring of financial performance. (Petar, Kukec & Turković, 2024)

The European Union does not have a unified legal framework for franchising, leaving individual member states to regulate it. This also applies to Croatian franchise systems that intend to internationalize their business in European Union countries. As a result, franchisors must understand the franchising regulations of each member state, which creates technical barriers to trade and growth.

To address this, there is a trend towards self-regulation in Europe, with national franchise associations developing codes of conduct. However, these efforts, often led by franchisors, may not fully address the balance of power between franchisors and franchisees, and their effectiveness varies across different countries.

Regulations governing this area in the Republic of Croatia can be divided into general regulations that govern the business operations of entrepreneurs and specific regulations that regulate the operations of particular industries. Among the general regulations, the most important are the Companies Act, the Crafts Act, and the Trade Act. The fundamental tax regulations include the Corporate Income Tax Act, the Personal Income Tax Act, and the Value Added Tax Act. Every entrepreneur, with the assistance of lawyers and consultants, should take the necessary actions to align their business operations with the regulations of both the host country and the target market.

The authors suggest that franchising offers numerous benefits to franchisors, including the ability to achieve rapid growth by expanding into new locations with limited use of their own resources. This model, in the author's view, also mitigates risk by transferring some financial and operational responsibilities to the franchisee. It also increases revenue through new income streams from franchising fees, sales commissions, and other fees. The scalability of the business through a franchising network allows expansion on a national or international scale. Furthermore, franchising strengthens the brand by expanding its presence across different markets, enhancing its recognition and attractiveness to other consumers. Sharing experience and resources with franchising partners can improve the business operations and success of both the franchisor and all business units. It also reduces operational costs, primarily including rental and staff salaries, which shifts the burden to the franchisor.

The authors assert that establishing controlled standards through the franchising business system is essential for preserving consistency and quality across all franchising units. However, despite these advantages, franchisors also bear certain responsibilities and risks, including the loss of control over individual franchising units as they expand. Different franchising partners may interpret standards and guidelines differently, which can lead to variations in quality and service. There is a risk associated with choosing unsuitable franchising partners, which can be detrimental to both the brand and the operations of the franchisee and franchisor. Poor partners can diminish the brand's reputation and lead to decreased demand and pricing of products/services, resulting in financial losses.

In the authors' opinion, the franchisor has an obligation to provide adequate support to franchise partners to ensure their success, which includes training, marketing support, operational assistance, and continuous communication. The costs of establishing and maintaining a franchising network can be financially demanding for the franchisor, including legal services, the creation of franchises, development of franchising manuals, contracts, marketing plans, and a management system for the franchising network. Internal competition among franchising units within the same market can lead to conflicts and decreased profitability.

Maintaining consistency in product or service quality and operational standards can be challenging, especially when franchising units operate in different geographical areas. Dependence on the franchising model makes it vulnerable to changes in the industry or market. If the franchising model is not well-adapted to changes, problems can arise. Dependency on franchising partners can negatively affect the overall franchising network if partners do not meet expectations. There is a need for oversight of the franchising network to ensure that all partners adhere to standards and guidelines, which can require significant time and resources. The legal and regulatory obligations of the franchising business system can further increase the complexity of the franchisor's operations and potentially lead to legal issues if all regulations are not respected.

Franchising model often requires for franchisees to meet specific technical conditions.

Depending on whether the franchise involves the distribution of products or services, conditions such as the size of the business space, geographical location, and the size of the market defined by geographical boundaries may be prerequisites for obtaining a franchise. This is particularly important for well-established franchise systems and recognizable brands.

Different prerequisite requirements help maintain the brand's consistency, ensure adequate customer reach, and optimize operational efficiency. By meeting these technical conditions, the franchisee aligns with the franchisor's strategic objectives, helping to maintain brand integrity, optimize market coverage, and ensure the overall success of the franchise network.

The authors believe that it is crucial for franchisors to carefully consider all relevant factors and to implement effective monitoring and support strategies to ensure the success of their franchising network. Effective governance in the franchising model also necessitates a robust legal framework to address the inherent challenges and mitigate the potential risks mentioned. Proactive legal strategies and compliance systems are essential to safeguard both the franchisor and franchisee, ensuring that the franchise operations adhere to national and international laws and standards. This framework helps to prevent legal disputes and maintain the integrity of the franchising system (Seid & Alon, 2011)

To optimize the franchising model's success, franchisors should focus on building a strong, communicative relationship with each franchisee. This relationship should be grounded in mutual respect and shared goals, with regular evaluations to ensure alignment and address any discrepancies in understanding or performance. Technology can play a pivotal role in this aspect by enabling better communication, streamlining operations, and providing real-time analytics and support (Morgan & Strong, 2003)

Furthermore, the evolution of the franchising network should be aligned with continuous improvement and innovation practices. This approach ensures the network's adaptability to changing market conditions and consumer preferences, which are crucial for long-term sustainability. It involves regular updates to training programs, operational procedures, and marketing strategies, which will keep the franchise network competitive and relevant (De Bono, 2002).

Additionally, strategic market analysis and careful partner selection are paramount. The franchisor should conduct thorough due diligence before selecting franchisees to minimize the risk of mismatches and maximize the likelihood of mutual success. This process should assess the potential franchisee's market knowledge, operational capabilities, and alignment with the franchisor's brand values and business goals (Kahn, 1988). In the context of intercultural communication, cultural adaptation directly impacts effectiveness (Wenwen, 2011).

Lastly, the franchisor must also maintain a balance between network expansion and quality control.

Rapid expansion should not compromise the quality standards set by the franchisor. Regular audits and compliance checks across the franchising network are vital to ensure that all units meet the established standards of quality and service. These measures help preserve the brand's reputation and consumer trust, which are integral to the franchisor's success in the competitive market (Welsh & Alon, 2001).

In conclusion, while franchising presents a lucrative avenue for business expansion, it requires a strategic and structured approach to management, support, and governance to harness its full potential effectively. The continuous evaluation and adaptation of the franchise strategy in response to operational feedback and market changes are essential for sustaining growth and maintaining competitive advantage in the market.

From the perspective of the franchisee, there are numerous advantages compared to starting a business independently. Key benefits for franchisees may include:

- **Proven Business Concept:** Adopting a business concept that has already proven successful in the market reduces the risk of failure compared to starting a business from scratch. This proven success offers a safer investment for new entrepreneurs, minimizing the uncertainty inherent in new ventures (Seid & Alon, 2011).
- **Brand Recognition:** Franchisees gain access to a well-known brand and reputation, which can attract a larger customer base and facilitate the building of trust in the market. This recognition is invaluable in drawing in customers who are already familiar with the brand, thereby accelerating market penetration and profitability (Morgan & Strong, 2003).
- **Operational Guidelines and Support:** Franchisors provide detailed operational guidelines and support to franchisees, including training, marketing support, and access to business knowledge and experience. This comprehensive support structure is designed to ensure that franchisees have all the tools necessary for success right from the start, helping them navigate the complexities of business operations efficiently.
- **Site Selection Assistance:** The franchising system often aids in selecting the optimal location for business, which can be critical for success. Strategic location choices enhance visibility and accessibility, directly influencing customer footfall and overall business performance.
- **Supplier Network Access:** Franchisees often have access to established suppliers and the bargaining power that comes with the size of the franchise chain. This can result in better pricing and terms for supplies, significantly reducing overhead costs and improving profitability.
- **Marketing and Advertising Support:** The franchising system typically provides marketing and advertising support, including national and local campaigns that can increase brand visibility and attract more customers. This orchestrated approach to marketing greatly enhances individual marketing efforts, providing a competitive edge in the marketplace.
- **Ongoing Support and Training:** Franchisors provide continual support and training to help franchisees manage their businesses and address challenges that may arise. This ongoing relationship ensures that franchisees remain updated on best practices and industry trends, maximizing their chances for success (Seid & Alon, 2011).
- **Reduced Risk:** While franchisees operate their own businesses, they do not bear the full risk associated with independent business ventures. Franchises usually allow for a faster start-up as much of the concept and strategy is already in place and tested. This significantly lowers the barriers to entry and operational risks (De Bono,2002).

Given these advantages, franchisees often have a higher chance of success compared to independent entrepreneurs. However, it is important to note that the benefits of a franchise depend on the specific franchise system and industry. Potential franchisees should carefully research and consider all aspects before deciding to enter into a franchise agreement.

While franchisees can experience numerous benefits, they may also face various drawbacks. Here are some common disadvantages that franchisees might encounter:

- **Initial Investment:** Entering a franchise usually requires substantial initial investments, including a franchise fee, costs for equipment, inventory, marketing, and other expenses. These costs can be high and may take time to recuperate. The financial entry barrier might discourage potential franchisees with limited capital (Seid & Thomas, 2011).
- **Operational Guidelines:** Franchisees typically must follow operational guidelines and stand-

ards set by the franchisor. This can limit their autonomy in managing the business and making decisions, potentially stifling creativity and local responsiveness (Nathan, 2014).

- **Ongoing Fees:** Franchisees generally must pay monthly fees to the franchisor, which can further strain their finances. These regular royalties and marketing fees, while necessary for the franchisor's continuous support, can reduce the profit margin for the franchisee (Seid & Thomas, 2011).
- **Market Competition:** In the franchise system, a franchisee often shares the market with other franchisees of the same brand. Internal competition can be intense, which may complicate success, especially in saturated markets (Nathan, 2014).
- **Dependence on Franchisor's Reputation:** The success of a franchisee often depends on the reputation and image of the franchisor. If the franchisor's reputation deteriorates or if there are issues in their business, it can negatively impact the franchisee's operations (Seid & Thomas, 2011).
- **Flexibility Limitations:** Franchisees usually have less flexibility to adapt their business to local needs and trends because they must follow the guidelines and standards of the franchisor. This rigidity can prevent franchisees from effectively responding to local market changes (Nathan, 2014).
- **Dependency on Franchisor Support:** Franchisees rely on the support and resources provided by the franchisor. If the franchisor fails to offer adequate support or withdraws from the business, it can create significant problems for the franchisee (Seid & Thomas, 2011).
- **Contractual Changes and Exit Difficulties:** Franchise terms can change over time, including fees, contract conditions, and operational guidelines. This can create uncertainty for the franchisee. Additionally, difficulties in exiting the franchise can arise if a franchisee wants to close or sell their business, potentially facing certain restrictions and obligations under the contract (Nathan, 2014).

Before deciding to take on a franchise, potential franchisees must research and weigh the advantages and disadvantages to get a fuller picture of what to expect.

Potential franchisees should thoroughly understand the financial structure of fees before investing. The initial franchise fee is an upfront investment for entering the franchise system, covering rights to the brand, business model, and initial support. Royalties, regular fees derived from the franchise's revenue, compensate the franchisor for ongoing support and the right to use the brand. Marketing fees fund joint marketing initiatives, strengthening the brand and boosting sales across all locations. Franchise agreements may include additional fees for contract renewal, transfer of rights, technological support, and specialized training, each aimed at optimizing operations and maintaining brand standards (Seid & Thomas, 2011).

The synergistic action of interconnected elements within the franchise ecosystem collectively facilitates, supports, and enhances the growth and success of the franchise model, bearing positive implications for the economy at large. Investments in business expansion create new business entities, generating new jobs and increasing fiscal revenues. Consumers have access to goods and services of standardized quality according to the franchisor's specifications to ensure consistency across the franchise network. However, standardized high-quality products and services under a well-known brand can negatively impact local merchants or service providers who are unable to compete. Market competition may lead to business closures and job losses for local entrepreneurs, and increased prices for consumers (Nathan, 2014).

3. Internationalization of franchising business

Determining the optimal strategy for expanding franchising business into international markets should answer the question of where, or to which country, to expand. An answer can be provided if we understand which internal or external factors significantly influence the success of franchising operations on international markets. Aliouche and Schlentrich have developed a methodology and conducted a ranking of 25 European Union countries according to their attractiveness from a macro perspective for US franchisors (Aliouche & Schlentrich, 2011). Considering limited resources, two factors—geographical and cultural distances—can be significant external factors in deciding which country to expand the franchising business into. Countries that are geographically closer require shorter travel times between two locations, which should mean lower costs for franchisee audits and lower goods delivery costs for distribution franchises. Lesser cultural distance is more likely in countries that are geographically closer, which can also significantly affect the lower costs of internationalizing franchising operations.

Internal factors that influence the internationalization of franchising business primarily include all company resources, whether they are financial resources, human resources, or technological equipment. Knowledge and expertise are important due to the understanding of international markets, language skills, and experience in international business. A high-quality organizational structure allows for flexibility, the ability to adapt quickly, and communication channel efficiency. Corporate culture signifies openness to innovations, willingness to learn, and adaptability.

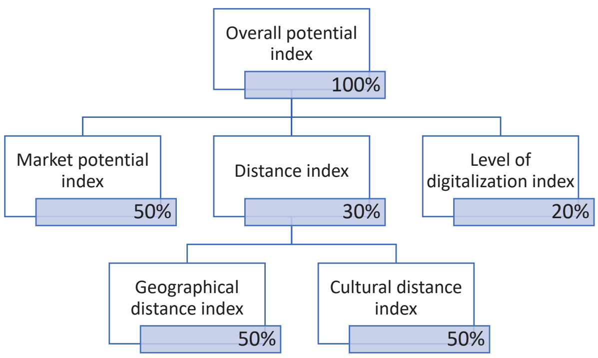
In relation to internal factors, external factors primarily include market dynamics, which entail the demand for goods or services, competition in the target market, market trends, and consumer preferences. The existence of demand for a product/service is one of the prerequisites for expansion into a targeted market. Cultural differences are also one the important external factors as values, customs, language, and consumer behavior can influence the success of the brand in the target market but also affect team functionality. Homogeneous teams are more functional in the short term but achieve the same results in the medium term (Roberts i sur., 2020). Regulatory frameworks such as legal restrictions, regulations, tariffs, and trade agreements can significantly affect certain goods or services. Economic and political factors such as stability, economic climate, and political tensions influence the decision-making and choice of internationalization strategy. Understanding and strategic adaptation to these factors is crucial for successful expansion into international markets and adapting products or services to the specifics of each market.

Small companies, if they are less successful in attracting franchise partners, will first have to focus on developing their own branches before expanding through franchising into international markets. (Alon, 2001). When entering international markets, it is important to choose an adequate strategy between standardization or adaptation of products and services. Standardization refers to the application of the same products, marketing strategies, and business operations regardless of local market differences. On the other hand, adaptation involves adjusting products, promotions, and operations to the specificities of each market, including culture, language, and consumer habits. The choice between these two strategies depends on many factors such as the nature of the product or service, corporate objectives, market characteristics, and the degree of international expansion.

Understanding cultural differences is essential for the successful internationalization of business and the expansion of franchises to new markets. Cultural adaptation in the context of integration into a new cultural environment requires knowledge of cultural norms, behaviors, and values that are being adapted. Openness to new cultures and flexibility in understanding culture, as well as potentially knowing the language, contribute to faster cultural adaptation. Understanding cultural distance in the context of franchising business on international markets is important for adjusting business models and marketing strategies in practice. Adequate adaptation to cultural differences brings products and services closer to local consumers, increasing effectiveness. Companies operating in international markets should consider developing cultural competencies and bridging cultural differences also from the perspective of partnership, and employee relations to ensure effective communication and relationships with local stakeholders (Hill & Hult, 2016). An additional factor to consider is that a successful mark in one country may be a disaster in another. Cases exist where a mark in one language is offensive in a foreign language. (Mendelson, 1992)

4. Methodology of the research

The methodology of this paper is designed to create indices using secondary statistical data, which will make market opportunities, cultural and geographical distance, as well as the level of digitalization visible to entrepreneurs. This approach aims to assist them in deciding how to allocate scarce economic resources when determining which international markets to expand their franchise business into.



Source: Authors

Graph 1. Index Development

The image shows the development of the overall potential index from its constituent components. The figure illustrates the step-by-step process of creating the overall potential index. The graph breaks down the index into its constituent components, showing how each element contributes to the final index value. This visual representation highlights the methodology used to combine various data points, such as market opportunities, cultural and geographical distances, and levels of digitalization, to form a comprehensive index that can be utilized in strategic decision-making for franchise expansion.

Quantifying geographical distance is relatively simple as the distance between two locations—in this case, between the Republic of Croatia and the target market. Countries with shorter distances were ranked higher. This research utilized the distances between the capitals of the countries included in the study.

Cultural distance was ranked using Hofstede's tool for comparing countries, developed according to (Hofstede, 2001), which considers six dimensions. Power distance addresses the fact that individuals in societies are unequal and reflects a culture's attitude toward these inequalities among us. It is defined as the extent to which the less powerful members of institutions and organizations within a country expect and accept that power is distributed unequally. Individualism looks at the level of interdependence a society maintains. It involves whether individuals emphasize personal independence or group membership. In individualistic societies, people are expected to look after themselves and their immediate families, while in collectivistic societies, they belong to groups that provide support in exchange for loyalty. Achievement motivation indicates a society driven by competition and achievement, marked by a high score on this dimension, whereas a low score signifies dominant values of caring for others and quality of life. Uncertainty avoidance relates to how society reacts to the unpredictability of the future: will we try to control the future or leave it to chance? Different cultures have developed various strategies to cope with this uncertainty, reflecting how threatened members of a culture feel in ambiguous situations and the extent to which they have developed beliefs and institutions to avoid them. Long-term orientation describes how societies balance maintaining links with the past while dealing with present and future challenges. Societies with low scores prefer preserving traditions, whereas those with high scores tend towards a pragmatic approach, encouraging savings and modern education to prepare for the future. Indulgence versus restraint addresses the challenge faced by human societies in socializing with their children. This dimension describes the extent to which people control their desires and impulses, stemming from their upbringing. Weak control is called indulgence, while strong control is termed restraint. Cultures can be described as indulgent or restrained. Hofstede Insights (2024)

The level of digitalization describes the extent to which processes, services, or business structures have transitioned to using digital technologies. This includes the presence of digital tools, infrastructure, ability to use technology, and acceptance of digital changes across different sectors of society or organizations. The term "digitalization" comes from the English word " digitalization " and can literally be translated as the process of converting information into digital form. This enables the automation and optimization of processes and improves communication channels between a company and its consumers. (Panchenko & Dovhenko, 2023) For this paper, the authors calculated the degree of digitalization of the entities being studied.

The "Global Market Potential Index 2022" is a tool used to rank countries based on their attractiveness for international business. It evaluates various factors such as economic stability, market size, openness to trade, infrastructure quality, and regulatory environments to determine the potential for business expansion and operations in different nations. Based on available statistical data, research was conducted on the global market potential, and the Global Market Potential Index for the year 2022 was calculated. The methodology for this calculation is shown below.

Dimensions and Measures used for the calculation, their importance weights, and statistical data included of Market Potential for 2022 as follows:

- Market Size (MS) weights 25%: Electricity Consumption (2021), Urban Population (2021)
- Market Intensity (MI) weights 15%: GNI per Capita Estimates Using PPP (2021), Private Consumption as a percentage of GDP (2021)
- Market Growth Rate (MGR) weights 12.5%: Compound Annual Growth Rate (CAGR) of Primary Energy Use (2016-2021), Compound Annual Growth Rate (CAGR) of GDP (constant 2005 US$) (2016-2021)

- Market Consumption Capacity (MCC) weights 12.5%: Consumer Expenditure (2021), Income Share of Middle-Class (2019), Median Disposable Income per Household (2021).
- Commercial Infrastructure (CI) weights 10.0%: Airport Connectivity (2020), Cellular Mobile Subscribers (2021), Fixed Broadband Subscriptions (2021), Fixed Broadband Internet Speed (2021), Logistics Performance Index (LPI) (2021), Paved Road Density (2021), Population per Retail Outlet (2021)
- Market Receptivity (MR) weights 10.0%: Per Capita Imports from US (2021) Trade as a Percentage of GDP (2021)
- Economic Freedom (EF) weights 7.5%: Economic Freedom Index (2021), Political Freedom Index (2021)
- Country Risk (CR) weights 7.5%: Business Risk Rating (2022), Country Risk Rating (2022), Political Risk Rating (2022)

Statistical data calculated as the average ranking in the column Overall score (OS) for the year 2022 presented in Table 1 reveal the three largest markets: China, India, and Brazil. The leading countries by Market Consumption Capacity are China, Japan, and Germany, while the leading countries with the lowest Country Risk are Norway, Denmark, and Japan. China, Singapore, and Hong Kong top the overall score. It is important to note that among the top ten leading countries by overall score, half are European countries. This is particularly significant as European countries are geographically and culturally accessible to Croatian entrepreneurs.

Comparison of countries based on cultural differences and geographical distance.

A comparison based on cultural differences was made using Hofstede's tool available on the website https://www.hofstede-insights.com/. Neighboring countries Hungary and Slovenia were taken into consideration as well as Austria.

Figure 2 shows the differences, but also the similarities between the countries. The results for Power Distance show a high score for Croatia 73, like Slovenia but in contrast to Austria, represents an acceptance of centralization and autocratic rule. Individualism in Croatia's score 42 show, in contrast to other observed countries, that it is a collectivist society. Croatia scores 40 In Motivation does not show a focus on well-being in contrast to Austria and Hungary. Croatia scores 80 very high but also other countries on Uncertainty Avoidance have a very high preference for avoiding uncertainty. The score for Croatia 40 does not indicate Long Term Orientation. Indulgence score of 33 for Croatia similar to Hungary and in contrast to Austria as Croatia like a Restrained country.

Source: https://www.hofstede-insights.com/

Graph 2: Cultural comparison of the countries Austria, Croatia, Hungary, and Slovenia

Using a procedure developed by (Kogut & Singh, 1988), we computed the cultural distance between Croatia and EU countries as follows:

$$CDj = \sum_{i=1}^{6} \frac{(I_{ij} - I_{RH})2/Vi}{6}$$

where I_{ij} stands for the index for the i-th cultural dimension and j-th country, V_i is the variance of the index of the i-th dimension, I_{RH} indicates Croatia, and CD_j is cultural difference of the j-th country from Croatia.

Geographical Distance and Cultural Distance in Assessing Market Potential

Geographical Distance: Geographical distance is based on the number of travel hours between the capital of the Republic of Croatia and the capitals of the relevant countries, using data obtained from maps.google.com.

Cultural Distance: Cultural distance is ranked using data available from (Hofstede Insights, 2024) which provides an analysis based on several cultural dimensions that impact business interactions.

Digitalization: The third key component for effectively determining the potential of a modern business market is the degree of digitalization. This paper considers various levels of digital intensity crucial for the internationalization of business, focusing on SMEs with at least a basic level of digital intensity and digital public services for businesses in target markets.

These elements are integral in evaluating the suitability and strategic potential of international markets for business expansion.

Digital Intensity Score and Its Impact on Internationalization

Digital Intensity Score: The digital intensity score is based on how many out of 12 selected technologies are utilized by businesses. The basic level requires the use of at least four technologies. The unit of measure are percentage of enterprises. Digital Decade DESI visualization tool, 2023.

Digital Intensity Index: A high digital intensity index in the target country can significantly facilitate and enhance the process of business internationalization, providing companies with technological, operational, and strategic advantages that are crucial for success in the global market.

Digital Public Services: Another particularly important component of the digitalization level in the target market relates to digital public services for businesses. The figure shows the ranking of EU countries according to the index of availability of digital public services.

These factors collectively contribute to the digital readiness of a market, influencing the ease and effectiveness with which businesses can operate and expand internationally.

The Role of the Online Public Services Indicator in Facilitating International Business

The indicator generally reflects the proportion of public services necessary for starting a business and conducting regular business operations that are available online for both domestic and foreign users. Services provided through portals receive a higher score, while services that only offer information (but must be completed offline) receive a limited score.

The availability of online public services for starting and conducting business is extremely important for companies planning to internationalize their franchising operations for several key reasons:

1. **Simplification of Processes:** If the necessary services for establishing and managing a business are available online, companies can more easily and quickly access relevant information and services without the need for physical visits to government offices. This can significantly reduce the time and costs associated with administrative procedures.
2. **Adaptation to Diverse Users:** An indicator that includes both domestic and foreign users demonstrates that the system is adapted to different needs and requirements, which is particularly important for international actors who may not be familiar with local procedures.
3. **Transparency and Predictability:** The online availability of services increases the transparency of the business environment. Companies can plan and prepare the necessary documents and procedures in advance, reducing the risk of unforeseen delays and complications.
4. **Market Competitiveness:** Countries that offer high-quality online services attract more foreign investment because they are considered more efficient and open for business. This

can be a decisive factor for companies when choosing a new location for expansion.

5. **Improved Access to Information:** Online platforms often provide comprehensive information that is crucial for compliance with local laws and regulations. This allows companies to be better informed and properly aligned with market requirements.

Due to all these reasons, a high score on this indicator can significantly facilitate and encourage the internationalization of business, making the process more efficient, predictable, and less demanding.

5. Results

The research outlined in this study presents a comprehensive analysis of the factors that influence the strategic decision-making process for the international expansion of franchising. Using the Global Market Potential Index for 2022 displayed in Table 1, the Distance Index in Table 2, and the Digitalization Index in Table 3, we have derived a nuanced understanding of how geographical proximity, cultural differences, and technological readiness impact market attractiveness.

Global Market Potential Index for 2022: This index offers insights into the overall attractive-

Table 1. Global Market Potential Index 2022

Rank	Country	MS	MGR	MI	MCC	CI	MR	EF	CR	OS
1	China	100	87	1	100	100	10	27	66	100
2	Singapore	2	52	60	59	79	100	82	94	51
3	Hong Kong	2	40	89	58	85	86	42	78	46
4	India	37	67	22	39	46	10	54	51	45
5	Canada	6	40	57	63	52	54	92	94	42
6	Ireland	1	88	37	52	47	42	98	82	40
7	Japan	13	29	49	77	72	14	84	94	40
8	Switzerland	2	42	66	68	61	40	100	77	39
9	Netherlands	3	42	44	56	69	44	95	94	38
10	Germany	8	32	55	69	60	23	91	88	37
11	South Korea	7	51	39	51	66	20	83	94	36
12	Denmark	1	52	55	50	61	25	93	100	36
13	Belgium	2	38	51	56	64	38	84	88	35
14	United Kingdom	6	28	64	67	59	18	87	82	34
15	Australia	4	43	55	66	43	19	93	94	34
16	France	7	36	52	61	62	16	77	88	34
17	Norway	2	45	56	57	48	22	92	100	33
18	UA Emirates	2	43	52	68	60	38	51	73	33
19	Estonia	1	60	38	39	46	29	95	88	32
20	Israel	2	55	45	61	51	18	73	86	31
21	New Zealand	1	46	56	48	49	16	96	94	31
22	Austria	2	40	55	54	50	22	88	88	31
23	Lithuania	1	58	51	33	46	28	88	82	31
24	Sweden	2	40	47	52	51	20	93	94	31
25	Italy	5	34	56	56	55	15	79	82	31
26	Poland	3	57	45	42	51	22	77	80	31
27	Slovenia	1	51	44	46	47	29	82	88	31
28	Spain	5	31	48	53	62	16	82	88	31
29	Slovakia	1	40	44	53	49	31	84	82	30
30	Cyprus	1	53	58	34	48	27	87	74	30
31	Finland	2	40	52	50	45	18	93	94	30
32	Czechia	2	43	34	45	52	27	89	82	29
33	Vietnam	4	85	8	26	52	31	57	51	29
34	Hungary	2	57	31	39	52	28	69	74	28

35	Portugal	2	37	57	37	55	18	85	88	28
36	Indonesia	11	67	22	26	41	10	66	66	28
37	Mexico	9	44	43	26	43	27	62	60	27
38	Romania	2	54	51	40	47	17	75	62	27
39	Chile	2	51	42	17	55	19	89	80	27
40	Malaysia	3	52	39	27	53	26	64	69	27
41	Qatar	1	45	53	52	45	25	55	60	26
42	Latvia	1	46	42	33	40	23	87	80	26
43	Brazil	15	47	33	18	45	11	57	47	26
44	Croatia	1	44	46	42	41	20	79	62	25
45	Greece	2	32	59	39	50	18	72	66	24
46	Guatemala	1	67	65	24	37	14	59	45	24
47	Ghana	2	98	38	15	22	12	67	33	24
48	Serbia	1	55	44	32	45	21	64	45	23
49	Russia	13	48	28	36	52	12	36	7	23
50	Thailand	4	46	21	26	65	22	47	63	23
51	Cambodia	1	100	29	15	32	22	40	30	23
52	Philippines	4	60	49	14	36	13	59	57	23
53	Egypt	4	62	73	28	38	9	31	37	23
54	Turkey	6	63	37	23	45	16	43	31	23
55	Costa Rica	1	54	40	10	44	26	79	51	23
56	Cote d’Ivoire	2	88	31	19	33	11	57	39	22
57	Uruguay	1	47	29	27	51	14	84	60	22
58	Panama	1	51	35	24	46	20	73	51	22
59	Bangladesh	5	85	37	19	33	4	41	38	22
60	Pakistan	6	71	60	26	30	8	37	15	22
61	Bulgaria	1	42	40	20	42	22	79	62	22
62	Peru	3	54	30	19	41	14	71	66	21
63	Bahrain	1	52	34	36	56	27	42	21	21
64	Saudi Arabia	5	37	32	45	48	15	32	61	21
65	Kuwait	2	28	42	43	41	20	47	69	20
66	Colombia	4	51	49	1	48	12	67	46	20
67	Dominican Republic	2	49	45	22	35	18	64	48	20
68	Honduras	1	60	60	10	27	21	55	41	20
69	El Salvador	1	44	62	24	37	20	58	24	19
70	Jordan	2	52	64	20	34	16	46	28	19
71	Morocco	2	56	21	18	41	16	48	55	19
72	Ukraine	3	42	44	34	41	16	55	11	18
73	Kazakhstan	2	58	29	23	40	13	48	38	18
74	Uzbekistan	2	75	23	16	37	13	35	36	18
75	Belarus	2	61	23	33	46	23	29	7	18
76	Kenya	2	65	46	16	30	9	47	24	17
77	Nicaragua	1	63	45	22	29	14	37	15	16
78	South Africa	4	28	31	20	40	13	63	42	16
79	Oman	1	40	24	37	40	16	42	36	16
80	Sri Lanka	1	54	46	13	47	10	48	7	15
81	Azerbaijan	1	53	19	19	38	15	39	48	15
82	Argentina	4	30	41	30	43	10	56	10	15
83	Tunisia	1	39	49	17	35	17	55	18	15
84	Bolivia	1	54	36	14	35	13	42	27	15

85	Nigeria	7	39	25	27	28	8	46	18	14
86	DR Congo	3	67	28	23	13	15	26	15	14
87	Ecuador	2	43	30	11	37	13	58	27	14
88	Cameroon	2	58	41	14	24	9	35	24	13
89	Uganda	2	62	39	9	19	10	40	30	13
90	Ethiopia	2	75	38	15	1	8	35	15	13
91	Tanzania	2	70	15	10	12	9	49	27	12
92	Paraguay	1	16	36	15	36	15	64	44	12
93	Algeria	3	51	1	17	33	11	30	38	11
94	Lebanon	1	1	100	20	32	17	38	7	11
95	Angola	2	65	7	3	21	12	38	24	10
96	Venezuela	3	36	NA	13	24	NA	1	1	2
97	Cuba	1	26	18	24	25	1	6	1	1

Source: https://globaledge.msu.edu/mpi/data/2022

ness of markets based on economic, political, and social parameters. The results indicate that European markets, with their stable economic environments and high consumer purchasing power, provide substantial opportunities for franchise expansion. Particularly, the markets with higher rankings in this index suggest a robust potential for business growth and profitability.

Distance Index: The geographical analysis shows that closer markets tend to facilitate easier management and coordination of international operations, reducing logistical costs and simplifying supply chain complexities. The proximity also enhances the ability to monitor and manage overseas operations more effectively, proving particularly advantageous for businesses looking to maintain high standards in franchise operations.

The results in Table 2 show the ranking of countries. Distance Index is calculated by computing an average of each country's geographic distance ranking and its cultural distance ranking and then ordering countries according to the resulting average. This results in Croatia being ranked first while Iceland is ranked last.

Table 2. Cultural and geographical distance —Index (2022).

Ranking	Country	Cultural distance / Score	Rank	Geographical distance / Hours	Rank	Composite score
Weight			50%		50%	
1	Croatia	0,0	1	0:00	1	1,0
2	Czechia	4,4	7	6:34	5	6,0
3	Romania	2,1	3	10:02	10	6,5
4	Slovenia	6,7	12	1:41	2	7,0
5	Bulgaria	1,7	2	11:48	13	7,5
6	Poland	3,1	5	10:06	11	8,0
7	Italy	5,6	10	8:58	8	9,0
8	Hungary	13,4	19	3:53	4	11,5
9	Greece	4,8	8	14:01	16	12,0
10	France	4,8	9	13:36	15	12,0
11	Spain	3,1	6	20:35	20	13,0
12	Germany	12,4	17	9:32	9	13,0
13	Luxembourg	8,9	15	11:21	12	13,5
14	Belgium	8,7	14	12:36	14	14,0
15	Switzerland	17,1	21	8:55	7	14,0
16	Slovakia	19,4	23	6:34	6	14,5
17	Portugal	2,2	4	25:00	26	15,0
18	Lithuania	7,2	13	15:06	17	15,0

19	Austria	25,4	27	3:10	3	15,0
20	Malta	6,7	11	21:50	22	16,5
21	Estonia	10,1	16	20:51	21	18,5
22	Latvia	13,3	18	18:14	19	18,5
23	Norway	18,2	22	23:52	23	22,5
24	Denmark	31,7	29	16:16	18	23,5
25	Finland	13,6	20	28:00	28	24,0
26	Netherlands	23,6	26	23:52	24	25,0
27	Ireland	19,4	24	26:00	27	25,5
28	Sweden	29,8	28	23:59	25	26,5
29	Iceland	21,1	25		29	27,0

Source: Authors

Digitalization Index: Our findings highlight the critical role of digital infrastructure in supporting business operations. Countries with a higher digitalization index offer more streamlined and efficient business processes, from registration and compliance to ongoing management tasks. Digital public services, as quantified in the index, significantly ease the bureaucratic burden on businesses, enhancing their operational agility and capacity to adapt to new markets.

Table 3 presents the rankings of countries based on their digitalization index in 2022, highlighting the level of digital infrastructure and services available for businesses. This index reflects the ease of accessing digital public services and other digital facilities crucial for business operations and international expansion.

The digitalization index is characterized by digital public services for businesses and the percentage of entrepreneurs who possess basic digital skills.

Table 3. Digitalization – Index (2022)

Ranking	Country	Digital public services score	Rank 1	% of enterprises	Rank 2	Compos. score
Weight			50%		50%	
1	Finland	100,0	1	89,5	1	1,0
2	Ireland	100,0	2	84,5	4	3,0
3	Malta	97,2	4	77,9	6	5,0
4	Denmark	88,7	9	88,8	2	5,5
5	Netherlands	89,4	8	80,1	5	6,5
6	Sweden	87,8	10	86,9	3	6,5
7	Estonia	98,8	3	66,9	15	9,0
8	Spain	91,0	7	67,5	12	9,5
9	Belgium	87,6	11	77,1	8	9,5
10	Luxembourg	96,7	5	66,2	16	10,5
11	Lithuania	94,4	6	63,7	17	11,5
12	Czechia	83,8	13	68,0	11	12,0
13	Portugal	81,9	16	70,3	9	12,5
14	Germany	80,7	18	77,3	7	12,5
15	Austria	82,9	14	67,3	13	13,5
16	Slovenia	82,7	15	67,1	14	14,5
17	Italy	74,7	22	69,9	10	16,0
18	Latvia	85,8	12	52,3	23	17,5
19	France	79,3	19	63,5	18	18,5
20	Slovakia	77,9	20	60,2	20	20,0
21	Bulgaria	80,8	17	47,2	25	21,0

22	Poland	72,7	24	61,0	19	21,5
23	Hungary	76,3	21	51,7	24	22,5
24	Croatia	66,8	25	57,8	21	23,0
25	Romania	44,6	26	52,5	22	24,0
26	Greece	73,7	23	41,2	26	24,5

Source: Authors

This index evaluates the extent to which the digital infrastructure supports business activities and the overall readiness of the workforce to engage effectively with digital technologies.

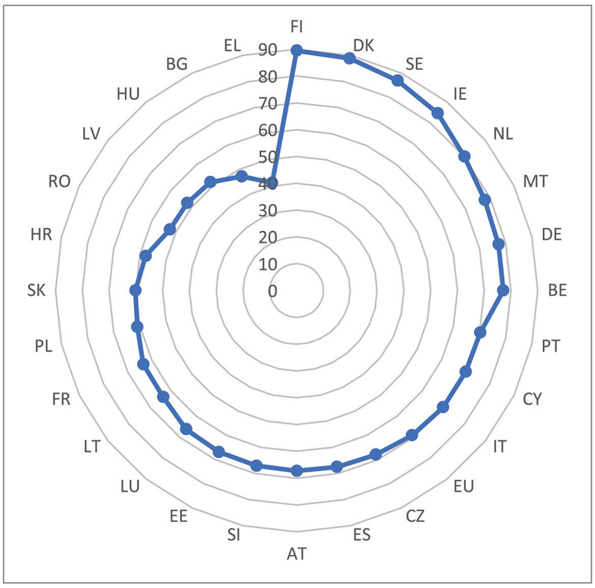
Graph 3 shows that there is a significant difference between the observed countries in terms of intensity, which varies from 40-90%. In 2022, Croatia with, a score 57,8 % (shown in Table 3) is among the countries with the lowest intensity, while northern countries like Finland, Denmark, and Sweden are at the top.

Graph 4 illustrates the ranking of EU countries based on the availability of digital public services for businesses in 2022, highlighting the varying levels of digital infrastructure and support provided to enterprises across the region. The research results in the figure show that Croatia is second to last, while Finland is at the top.

Franchising Potential in the European Union: Table 4 reveals the franchising potential of 24 EU countries, emphasizing the market dynamics from a Croatian perspective. The weighted methodology, attributing 50% to market potential, 30% to geographical proximity, and 20% to digital readiness, prioritizes these factors based on their perceived impact on successful franchise operations. This strategic weighting reflects an understanding that while market size and potential are paramount, the logistical and digital frameworks supporting market entry and operation are equally critical to sustainable success.

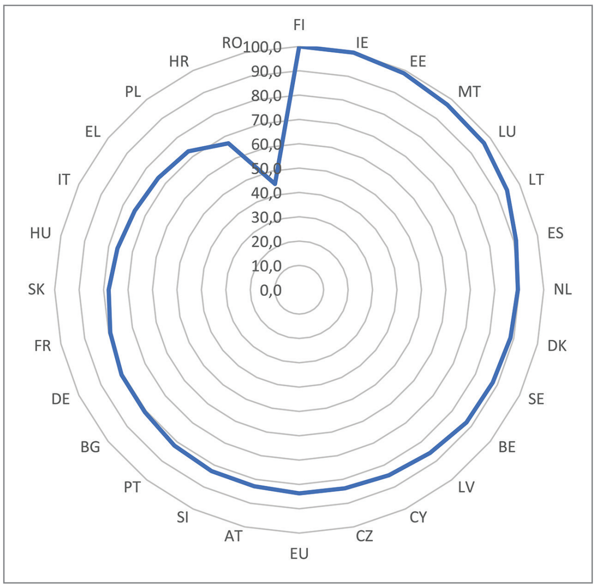
This research contributes significantly to the field by providing franchisors with a clear framework to evaluate potential international markets. The rankings not only guide franchisors on where to focus their expansion efforts but also underscore the importance of an integrated approach that considers economic potential alongside logistical and digital infrastructures.

These insights are particularly valuable for businesses contemplating expansion in an increasingly interconnected and digitally dependent global marketplace. By aligning franchise expansion strategies with the detailed metrics provided in this study, businesses can better position themselves to capitalize on emerging opportunities and navigate the challenges of international market entry.



Source: Digital Decade DESI visualisation tool, 2023

Graph 3. SME-s with at least a basic level of digital intensity – 2022



Source: Digital Decade DESI visualisation tool, 2023

Graph 4. Digital Public Services for Businesses – 2022

Table 4. Franchising Potential – Index (2022)

Ranking	Country	Pot. Ind.	Rank 1	Distance	Rank 2	Digital.	Rank 3	Compos. score
Weight			50%		30%		20%	
1	Germany	37	3	13,0	12	12,5	12	7,5
2	Ireland	40	1	25,5	23	3,0	2	7,8
3	Belgium	35	5	14,0	13	9,5	8	8,0
4	Netherlands	38	2	25,0	22	6,5	4	8,4
5	Denmark	36	4	23,5	20	5,5	3	8,6
6	France	34	6	12,0	10	18,5	17	9,4
7	Estonia	33	7	18,5	18	9,0	6	10,1
8	Slovenia	31	13	7,0	4	14,5	14	10,5
9	Italy	31	11	9,0	7	16,0	15	10,6
10	Czechia	29	17	6,0	2	12,0	10	11,1
11	Lithuania	31	9	15,0	16	11,5	9	11,1
12	Austria	31	8	15,0	17	13,5	13	11,7
13	Spain	31	14	13,0	11	9,5	7	11,7
14	Poland	31	12	8,0	6	21,5	20	11,8
15	Sweden	31	10	26,5	24	6,5	5	13,2
16	Finland	30	16	24,0	21	1,0	1	14,5
17	Slovakia	30	15	14,0	14	20,0	18	15,3
18	Romania	27	20	6,5	3	24,0	23	15,5
19	Hungary	28	18	11,5	8	22,5	21	15,6
20	Croatia	25	22	1,0	1	23,0	22	15,7
21	Portugal	28	19	15,0	15	12,5	11	16,2
22	Bulgaria	22	24	7,5	5	21,0	19	17,3
23	Greece	24	23	12,0	9	24,5	24	19,0
24	Latvia	26	21	18,5	19	17,5	16	19,4

Source: Authors

5. Discussion

Every company planning to expand into international markets can, depending on its own capacities and capabilities, determine the importance of specific parameters. It is essential to consider the particularities of individual franchising systems and industry specifics to ensure that the decision on selecting a location best fits the needs of the franchisor.

This customized approach allows businesses to align their expansion strategies with their operational strengths and market opportunities. By evaluating the relevance of various factors such as market potential, cultural and geographical distances, and digital readiness, companies can prioritize markets that offer the optimal mix of opportunities and manageable challenges.

Furthermore, understanding the unique requirements of their franchising model—whether it demands close cultural ties for brand consistency or relies heavily on digital infrastructure for operations—can significantly influence the decision-making process. This strategic alignment ensures that the selected markets not only promise growth but also align with the company's ability to deliver its business model effectively.

Thus, while global indexes and general market analyses provide a valuable starting point, the ultimate success of international expansion relies on a deep understanding of both the external market environment and the internal capabilities and strategy of the franchisor. This holistic approach to international expansion is crucial for navigating the complexities of global markets and achieving sustainable growth.

6. Conclusion

Expanding business into international markets represents a significant step for franchisors, requiring not only financial resources but also a deep understanding of the potential of target markets. Beyond the economic potential, a variety of factors play a crucial role in the successful internationalization of business. Geographic and cultural distances, along with the level of digitalization, are key factors that entrepreneurs must consider when selecting a location for their market. Additionally, the legal and political framework, as well as socio-economic stability, can significantly influence the choice and success in international markets.

The ability to assess a target market based on precise and relevant data can greatly facilitate entrepreneurs in planning their strategic decisions. As franchising continues to evolve and its expansion into international markets intensifies, further research will be essential to better understand the trends and success factors that Croatian entrepreneurs consider when entering new markets. This research should also encompass an analysis of market dynamics and consumer preferences in various regions, providing entrepreneurs with valuable insights and increasing the chances of success in their international operations.

By integrating these insights into a strategic framework, businesses can enhance their market entry strategies and operational effectiveness. The conclusion of this study underscores the importance of a methodical approach to international market analysis and the strategic alignment of market selection with the franchisor's capabilities and goals. In doing so, franchisors can not only mitigate risks but also maximize the opportunities presented by global expansion.

Instructions for Future Researchers and Research Limitations

This study acknowledges certain limitations, primarily from the current underdevelopment of Croatian franchise systems that are in the process of internationalization. The limited number of Croatian franchises that have successfully expanded into European markets restricts the ability to fully analyze the effectiveness and challenges of this process in a broader context.

Future researchers are encouraged to focus on these emerging franchise systems as they continue to grow and expand internationally. A key area for further exploration could involve studying how Croatian franchises are distributed across various European countries, identifying patterns, and understanding the practical implications of this expansion. Such research would provide valuable insights into the internationalization strategies of franchises and contribute to a more comprehensive understanding of the franchising landscape in Europe.

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