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How Franchising Helps Entrepreneurs Scale Faster and Build Market Dominance

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Research on restaurant chains shows why franchising can turn a proven business concept into a self-reinforcing growth engine.

First in a series on franchising

Competition in service industries that span wide geographies often occurs through chains—a single firm operating units in multiple locations with the same products, services, trademarks, and production systems. Frequently these chains are organized as franchises, where local entrepreneurs purchase the right to sell and operate one or several units from the owner of those trademarks, products, and systems. In return for a royalty on sales to the franchisor, the franchisee uses an established system and trademark and receives operating support.

Franchising is big business in the USA and worldwide. According to recent data from the International Franchise Association (IFA) and FRANdata, the U.S. franchise sector includes approximately 830,000–851,000 establishments, generates roughly $897–936 billion in annual economic output, and supports nearly 8.9 million jobs. Franchising contributes significantly to U.S. GDP (around 3%) and consistently outperforms the broader economy in growth. Globally, franchising powers millions of businesses and employs tens of millions, with one estimate suggesting it accounts for about one in seven businesses worldwide and contributes over $2 trillion to the global economy.

The U.S. restaurant industry, a major beneficiary of franchising, is projected to reach approximately $1.55 trillion in sales in 2026 while employing nearly 15.8 million people (National Restaurant Association, 2026). Restaurants constitute a substantial portion of the franchise sector—roughly one-quarter of all franchised businesses—with franchising playing an especially dominant role in quick-service and limited-service segments.

Franchising remains one of the most effective strategies for entrepreneurs and chain operators in service industries—especially restaurants—to scale rapidly, overcome resource constraints, and secure lasting competitive advantages. How should an aspiring chain entrepreneur choose to franchise, and if so, how? What mix of owned and franchised units should the entrepreneur employ? Two complementary streams of research provide clear, actionable guidance: one showing how franchising generates increasing returns to scale in growth, and the other demonstrating how it helps early movers build superior market positions that drive higher profitability.

UNDERSTANDING GROWTH DYNAMICS IN CHAINS

Economists have long studied firm growth through Gibrat’s Law (the Law of Proportionate Effect), which suggests growth rates are independent of firm size—essentially random. In manufacturing and most services, smaller firms often grow faster. Restaurant chains, however, behave differently due to their model of replicating standardized outlets through mixed governance (company-owned plus franchised units).

Economist Edith Penrose identified a foundational limit on growth: As a firm expands, it needs more managers who truly understand the business, can be trained quickly, and fit the culture. Finding, training, and integrating enough qualified people takes time and creates a bottleneck—the Penrose managerial capacity constraint. This often slows or caps expansion in company-owned models.

Data from Entrepreneur magazine’s Franchise 500 listings for over 1,300 restaurant chains (1979–2019) reveal how franchising changes the picture:

- Franchised units exhibit increasing returns. Larger chains grow faster than smaller ones when expanding through franchisees. Size itself becomes a self-reinforcing advantage.
- Company-owned units follow the more common pattern. Smaller operations tend to grow faster here, consistent with limitations on managerial talent.
- Overall chain growth follows the franchised pattern. With franchising typically making up about 77% of units, the entire business benefits from accelerating expansion.

These patterns hold for full samples, long-term survivors, pure franchising chains, and different ownership mixes. Franchising relaxes the Penrose constraint by drawing on franchisees' own capital, deep local market knowledge, and strong personal motivation to succeed. It also creates powerful network effects: More outlets boost brand visibility, customer familiarity, and the ability to attract high-quality franchisees.

In short, franchising turns scale into a virtuous cycle. Chains that use it—especially after proving the concept with initial company units—achieve faster, more sustained growth through increasing returns.

HOW FRANCHISING DELIVERS FIRST-MOVER ADVANTAGE

Rapid scaling via franchising does more than speed growth. It lets early entrants dominate markets. Research on restaurant chains outlines a clear three-step mechanism:

- **Franchising enables faster assembly of outlets.** By accessing external capital, local entrepreneurial talent, and motivated operators, franchising overcomes capital and managerial bottlenecks (including the Penrose constraint). Early movers can open locations quickly and claim prime geographic and market space ahead of competitors.
- **Having more outlets builds greater market share**. More locations increase brand exposure, customer familiarity, and consideration-set dominance: the tendency for consumers to limit their purchase decisions to a small set of familiar, trusted options. In everyday, low-involvement choices like fast food or casual dining, people rely on mental shortcuts: They choose brands they've seen repeatedly and feel they "know." A widespread network makes your chain top-of-mind, crowding out less-visible competitors. Prospective franchisees are also drawn to proven systems through social proof—the powerful human tendency to look at what others are doing (successful franchisees, crowded parking lots, positive word-of-mouth) as evidence that the opportunity is sound. This creates a self-reinforcing cycle and disproportionate market presence.
- **Higher market share drives superior profitability.** Greater share yields economies of scale in purchasing, advertising, and operations, stronger bargaining power with suppliers, and pricing power with customers. It also raises barriers for later entrants, protecting long-term returns.

Iconic fast-food leaders like McDonald's and KFC exemplify this sequence. Franchising allowed them to build widespread presence rapidly and lock in advantages that competitors have found hard to dislodge. This process reinforces the increasing-returns dynamic: Bigger networks draw more customers and franchisees, widening the lead over time.

IMPLICATIONS FOR ENTREPRENEURS AND CHAIN OPERATORS

Strategic sequencing is powerful. Start with company-owned units to refine the model and build credibility for franchisees. Once proven, emphasize franchising for rapid scaling and sustained momentum. The three-step first-mover process described above works best with this approach.

Plural-form organizations (a mix of owned and franchised units) provide flexibility. Use company units early for control and learning; shift toward franchising as you grow to capture increasing returns while managing capacity limits.

Power compounds over time. Growth-pattern simulations show striking differences over 20 years. A small chain following corporate-only patterns may reach only modest scale, while one leveraging franchising can grow several times larger—especially from a larger starting base under increasing returns.

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This path supports first-mover positioning. Faster outlet growth fills markets, strengthens the brand through consideration-set dominance and social proof, and delivers the share and profit advantages shown in the research.

KEY QUESTIONS BEFORE YOU FRANCHISE

About your concept and readiness:

- Is my model proven, easy to replicate, and attractive to both customers and potential franchisees?
- Do I have strong, documented systems for training, operations, support, and supply chains?

About timing and structure:

- How many company-owned units do I need to demonstrate viability?
- What ownership mix best fits my current stage and long-term vision?
- Am I ready to build the infrastructure that supports franchisees while safeguarding brand standards?

Due diligence and execution:

- Study growth trajectories and disclosure documents of comparable chains.
- Talk with current and former franchisees from other concepts and chains plus experienced franchise attorneys.
- Remember that franchising is a team sport. Both franchisee and franchisor must be successful for the chain to be successful.

SUMMARY

It is a natural question to ask whether this advice holds outside the restaurant industry, where the models and concepts were validated. Although other industries using chains were not studied in depth, the underlying theoretical mechanisms—such as building consideration-set dominance through multiple locations, driving market share via outlet share, creating network effects, and relaxing managerial constraints—are likely to apply in similar service-oriented settings with standardized, replicable operations. Casual observation and related research suggest comparable dynamics in sectors like auto repair, copy/print shops, fitness centers, lodging, and other retail/services where brand familiarity, local execution, and geographic coverage matter.

Franchising is much more than a way to raise capital. It is a proven approach for overcoming growth limits like the Penrose managerial bottleneck, for generating increasing returns, and for capturing first-mover advantages in competitive service markets. Through rapid outlet expansion, it creates a self-reinforcing cycle of brand strength, customer loyalty, franchisee recruitment, market-share leadership, and higher profitability.

Chains that thoughtfully combine initial company-owned units to prove the concept with aggressive franchising are well positioned to build large, resilient businesses. The combined research on growth dynamics and first-mover mechanisms is clear: When executed well, franchising offers one of the strongest paths to scale and sustained competitive advantage for services entrepreneurs.

Learn More

S.C. Michael & A.C.J. Porto, "Does Gibrat's Law Apply to Chain Organizations? The Case of Franchising, (https://www.tandfonline.com/doi/full/10.1080/00036846.2026.2613166) " *Applied Economics*, 2026

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The source of franchising statistics cited in this article is International Franchise Association & FRANdata, 2025–2026 Franchising Economic Outlook. The restaurant statistics come from the National Restaurant Association, State of the Restaurant Industry 2026.

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Week of June 15: How a franchisor's financial problems can affect local franchisees and their communities; and

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