DIAGNOSES

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Apollo Health and Lifestyle Limited: Retail Franchising in the Healthcare Industry

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This issue of *Vikalpa* has published a Management Case titled, **Apollo Health and Lifestyle Limited: Retail Franchising in the Healthcare Industry,** by Sanjay Patro and Vinay Kumar. This Diagnoses features analyses of the Case by Piyush Sinha, RC Natarajan, MN Tripathi, N Rajkumar, and Sanal Kumar Velayudhan.

Case Analysis I

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The case is relevant in terms of bringing out the concept and issues that the franchisees are facing. However, a lot of the conceptual framework would need to be understood before a systematic analysis can be put forward. From this perspective, it is a difficult case to teach. It describes the concept development and franchising plan well but does not provide enough information on the issues at hand. I would, therefore, address the case from a conceptual as also from an industry/company behaviour perspective.

Issue 1: Choice of Franchising as Mode of Entry

Franchising provides one of the best ways to enter the market for a company that is looking for rapid expansion. The case brings out this point very well. It is also the most commonly used form in service distribution as well as retailing. It is clear from the case that franchising does not require upfront investment from the company. This raises the stake of the franchisee who is expected to put in the right kind of efforts and be committed. The company is able to retain its control over brand value and processes so as to ensure a good quality of service delivery. More importantly, it does not 'outsource' customer management. The responsibility for ensuring customer satisfaction still stays with the company, which indeed is the most difficult task.

The basic difference between franchising and dealership lies in the focus—process *vis-à-vis* product. In case of franchising, the process of doing business and serving the customer is the key; it is assumed that a good process would lead to good delivery. Achieving this, however, is not easy. In case of franchising, practice is more integral to success than the policies. It requires regular implementation and developing a habit leading finally to an attitude of the provider that would in turn be followed by good practices in almost all situations. It is just not possible to create

such habits unless the franchisee portrays the same level of ownership as the company. All this needs that a benchmark is created, especially when a company is pioneering into a new business. In the absence of a benchmark, the company needs to develop its own benchmark. This has led to a thumb rule of 2 + 3 in franchising. In the initial years, the company must run 2 of the outlets on its own before franchising 3 of its new outlets. This is required for demonstrating a good quality service delivery.

Issue 2: How Big is the Market?

Market potential determination has always been a key to the success of a new venture. Let us take a classical way of determining the market size. We would consider the gross potential, conduct a study to find out the portion served by the existing players, and arrive at a potential that is available to the company. It is a very simple and robust method. However, we need to keep in mind two things to avoid being misled into a mirage. First, the Indian market is growing at an unprecedented rate opening new markets waiting to be harnessed. Second, how does one estimate a potential for a concept that the market has not experienced before. Keeping these facts in mind, Apollo has a greenfield market.

Unfortunately, market studies based on macro variables show a huge potential creating euphoria; the quest of being the first pushes many companies overboard. In addition, while the corporation may still remain sane in such a situation, most channel members tend to get carried away by the euphoric response and have high expectations. The point is these expectations may not be realistic. A company needs to be very careful at this stage and must explain the problem to the franchisees. Having a strong (highly recalled) brand adds to the euphoria and may in fact prove to be a disadvantage as the franchisees would tend to presume that this would wade them through rough times.

Another dimension of estimating the potential correctly is the level of detailed information available for the trading areas of each of the outlets. It must be understood that adoption of a brand by franchisees or customers is not restricted by geography, but purchase and consumption are. Besides the demographic profile of the trading area, several spatial and behavioural control factors play a role in selecting a clinic. The traffic pattern, parking facilities, timings, intensity of need besides pricing are some of the factors that customers would tend to consider before deciding to come to the clinic. The congruence between the customer's self-concept and the concept of the store is necessary for attracting repeat business. It is also found that for larger section of the population, visiting clinics is an 'unsought' practice. Several attitudinal, both affective and cognitive, factors create a gap between intention and actual purchase. It is commonly perceived that in highly potent markets, companies tend to take a leap based on only demographic information and ignore the lifestyle and attitudinal factors. It is difficult to measure them as customers have a tendency to respond on the basis of their current experiences and not necessarily on their new concept, leading to results that may not be the true reflection of the market potential.

Issue 3: Would the Company be Able to Sustain?

In the light of the above discussion, it may be prudent to say that clinics would need to create a favourable attitude among the target customers. This would require time and consistent delivery of the promises made. Unless the company has staying power this would not be possible. Also the business must start generating surplus in as short a span as possible at the clinic level if not at the corporate level. Experience indicates that one needs about 2-3 years before a clinic can be said to be stable.

Franchisees would also require to retain the fervour of carrying this business even if things do not turn out the way it was planned. This becomes particularly important as there are high chances that market estimations would go wrong while operating in a new market. Interestingly, most of the plans are optimistic in line with the growth in the marketplace. The strong market and positive sentiments supported by a strong brand leads to a very optimistic plan, with hardly any sensitivity analysis for the worst case scenario. Even the worst case scenarios tend to be optimistic. This leads to a target setting process based more on feelings than on market realities. In most cases, a higher level of investment is committed upfront leading to higher break-even points and a need to convert higher number of customers at a faster rate.

Issue 4: Does the Company have the Capabilities and Resources?

Once the company has estimated the market, it needs to create processes, systems, and resources for harnessing the potential. In case of Apollo, financial resources may not be an issue. But whether the knowledge of running a hospital can be transferred to clinics remains a crucial factor. And if the company has to find new capabilities, the parent organization support is useless. In fact, it may actually be detrimental. Companies build the required capabilities by running the operations on their own before handing over to the franchisees.

It should also be kept in mind that the value sought by a customer from a clinic is very different from that of a hospital. Therefore, even if Apollo is targeting its own hospital customers, they are actually not the same customers as the factors affecting their choice of a clinic would be entirely different, making them a different set of customers. It is also observed that very few companies are able to effectively manage the activities across the value chain, simply because the key success factors of each of the slivers are different and so are the capabilities required.

What Should Apollo do Now?

- Go back to basics.
- Recognize that the operations of the clinics cannot be managed with a macro perspective. Develop plans clinic by clinic and aggregate. Franchising is a bottom-up business.
- Recognize that it can not absolve itself of the responsibility of managing customers, even if the operations have been 'outsourced'.
- Enhance its commitments, financially or otherwise, and work with franchisees to address the problems.
- Determine customer value-based market segments and then devise delivery mechanism accordingly.
- Estimate markets more realistically. Check out the brand power; do not assume it.
- Work out revenue and cost targets along with the franchisees.
- If possible, run some/all of the clinics by itself before expanding.

Case Analysis II

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The Apollo case can be approached from the following three angles:

- Is there merit in Apollo's foray into primary and preventive healthcare segment?
- What is/are hampering AHLL's growth?
- What can be done to enable AHLL's growth?

Is there Merit in Apollo's Foray into Primary and Preventive Healthcare?

The Apollo group's foray into primary healthcare through AHLL can be justified as an appropriate move due to the following reasons:

- Apollo Hospitals are mainly super-speciality hospitals, with greater emphasis on tertiary healthcare that warrants highly technology-intensive and specialist-oriented surgical methods. Since such specialist surgeons are limited in India, the cost of expansion in tertiary (super-speciality) healthcare is very high, and hence expansion in tertiary healthcare is a limited prospect.
- Primary and preventive healthcare services in our country are still confined to middle and upper middle income groups,—as the case, too, points out—the rest visiting doctors only in times of illness. Even within this segment, the proportion of preventive healthcare is rather small, with most of the visits to doctors being during times of physical discomfort. Some of these cases turn towards secondary healthcare given the nature of illness; a few of them become serious and therefore are referred to tertiary healthcare. It is clear that (i) there is lack of aware-

ness about the importance of primary healthcare among people; and (ii) there is a need for primary, preventive healthcare. Expansion into this segment may (a) improve the quality of life of the large middle/upper middle income group, which can reduce a lot of hidden costs that the government, the public, and the commercial sectors incur due to illnesses; (b) increase the life span of people in India; and (c) reduce the strain on tertiary healthcare facilities enabling better utilization of the same. Hence, even from a social perspective, private investment in primary/preventive healthcare is a welcome move.

- As explained schematically in the Case, entry into primary healthcare can also generate the necessary goodwill for the Apollo brand, making Apollo Hospitals the first choice among customers requiring secondary and/or tertiary healthcare.

In addition to these three factors, which are mainly customer-based, the industry scenario too justifies Apollo's expansion into primary healthcare. Combining the data in the Case text about the availability of various health services and the data in Exhibit 4(b) (collapsed into *Quality* and *Economy*), we get a perceptual map that suggests the possible position of AHLL and Apollo Hospitals [Figure A].

The absence of information about the other corporate hospitals notwithstanding, we can at best surmise that they too must be overlapping with the position of Apollo Hospital in the perceptual map.

Figure A: Perceptual Comparison

Thus, we see that AHLL has a clear position of good quality and very good economy, where competition is absent, a phenomenon that can be leveraged upon.

The core strength, and therefore the offer of AHLL should be (which the Case says *is*) value for money. Thus, AHLL is in a sound position for Apollo to pursue, as it offers a distinct consumer-value that is unique in the competitive space, namely, "significantly superior service at competitive price" in the primary and preventive healthcare segment.

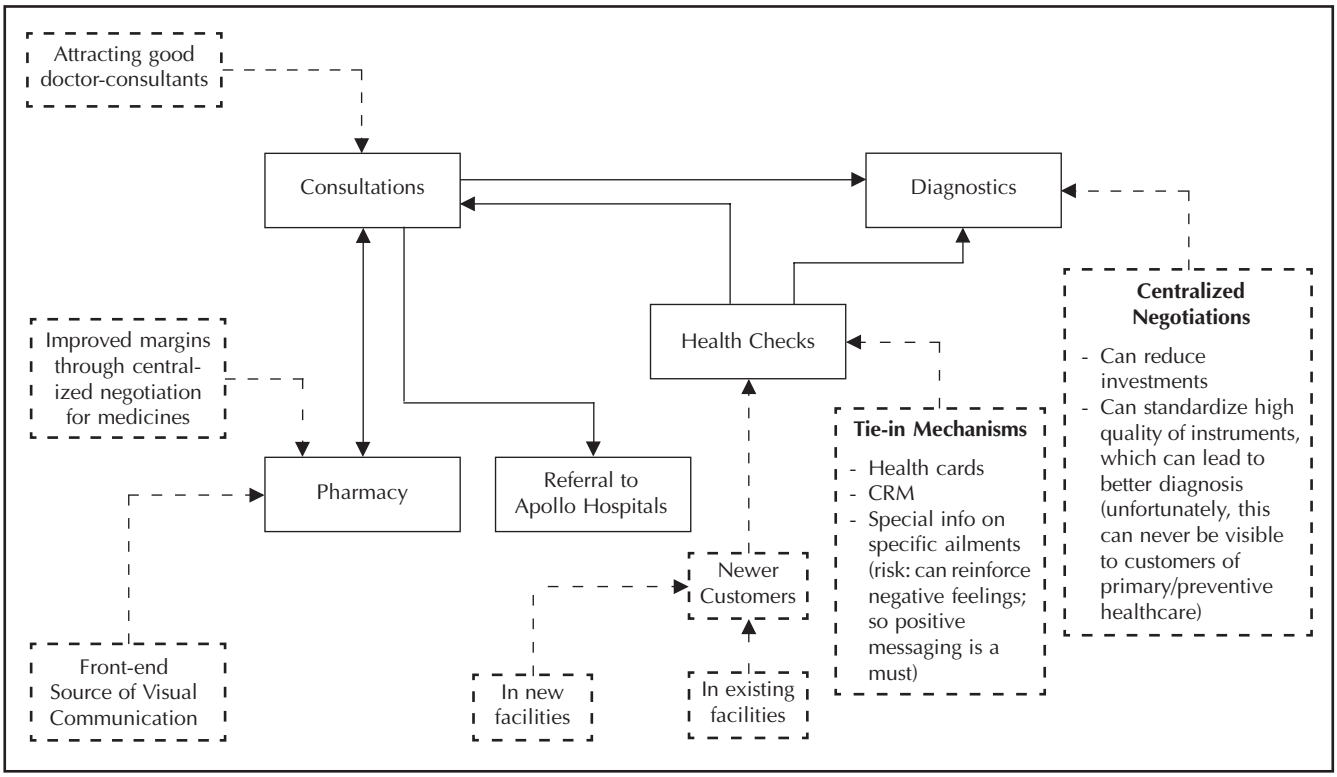
At this juncture, one has to be conscious of the fact that AHLL and Apollo Hospitals compete neither in the marketplace, nor in consumers' mind-space. AHLL plays in primary and preventive healthcare segment while Apollo Hospitals are in secondary, and more significantly, in tertiary healthcare segments. No doubt, there will be marginal cannibalization in Apollo Hospitals' OPD patients, which should be an inevitably acceptable eventuality. Aside the marginal cannibalization, AHLL can generate the goodwill that can cause the top of the mind recall of Apollo Hospitals, when AHLL's customers need secondary and/or tertiary healthcare subsequently. Thus, AHLL is a useful addition to Apollo's service-portfolio.

Strategically, too, the other hospitals will be unable to match the quality-economy mix that AHLL can offer due to (a) economy of scale and (b) economy of scope enjoyed by Apollo. Access to the latest knowledge in the medical field through Apollo Hospitals can serve as a visible source of attraction to the physicians in updating their knowledge through an association with AHLL.

What is Hampering AHLL's Growth?

In organizations such as AHLL, growth can be achieved either through increased margins or through increased volume (customers in this case). AHLL seems to have chosen the latter. Growth is aimed through increasing the reach. This growth strategy is akin to distribution-expansion in consumer goods sector, where it is said that a company cannot achieve consumer-diffusion until it achieves retailer-diffusion. Analogously, it can be seen that the channel is proving to be the bottleneck for AHLL, which leads us to the question: How can AHLL increase its franchisee-base? To answer this question, we need to ask another related question: What is preventing it? For this, we need to comprehend how AHLL's system

Figure B: How Franchise System Works for AHLL



works. This is done by expanding the schematic depiction given in the Case; we extend the diagram further, as shown in Figure B.

The interesting question is: Why is this system not working well for AHLL's expansion plan? A few reasons have been identified:

Break-even and accumulated losses: One of the answers possibly lies in the projections shown to the potential franchisees (Case Exhibit 2: *Projected Profit & Loss Statements*). Interestingly, the Exhibit shows the first year and the seventh year. The most simplistic assumption is to believe that the growth will be linear; but this is most unlikely to be so. Most often than not, any new business venture takes time to take off, grow and stabilize, taking the shape of an S-curve, as shown in Figure C. However, the costs are likely to grow linearly over the years. Since the Case is silent about the intermediary years, one is tempted to surmise that AHLL is possibly failing to present a correct picture to the franchisee-aspirants and perhaps jacking up their expectations, leading to disappointment, especially in the first three years. This message must have spread across various franchisee-aspirants who would have been discouraged to apply for the franchise.

These projections yield us the expected returns from the operations as shown in Table A, where it can be seen that the gestation-period is almost four years, a far cry for a franchisee who puts in his funds to reap rewards. The ROI reaches the decent level of 24 per cent only in the fourth year, the first three years incurring an accumulated loss. This is an important aspect of the franchi-

Figure C: Projected Revenue (Rs. Lakh)

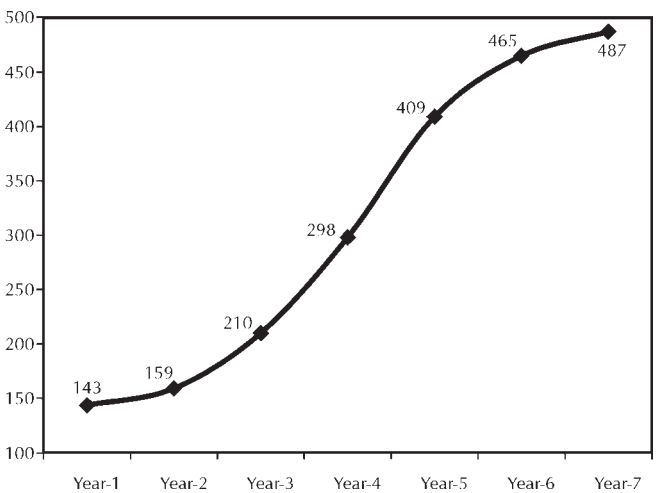


Table A: Projected P & L and Ratios

	Year-1	Year-2	Year-3	Year-4	Year-5	Year-6	Year-7
Gross Income	143.49	159.00	210.00	298.00	409.00	465.00	487.36
Direct Expenses:							
Materials cost (Purchases)	49.99	69.31	88.63	107.95	127.26	146.58	165.90
Payment to visiting consultants	9.90	13.98	18.05	22.13	26.21	30.28	34.36
Royalties & management fee to AHLL	7.17	10.04	12.90	15.77	18.64	21.50	24.37
Power, utilities and others	3.60	4.89	6.18	7.47	8.76	10.05	11.34
Total direct expenses	70.66	98.21	125.76	153.32	180.87	208.42	235.97
GROSS PROFIT	72.83	60.79	84.24	144.69	228.13	256.58	251.39
Indirect Expenses							
Personnel cost	23.28	26.24	29.19	32.15	35.10	38.06	41.01
Lease rentals for premises	9.60	10.14	10.69	11.23	11.77	12.32	12.86
Administrative expenses	4.80	5.42	6.03	6.65	7.27	7.88	8.50
Marketing & sales promotion	9.00	10.16	11.31	12.47	13.63	14.78	15.94
Others	1.60	1.81	2.01	2.22	2.42	2.63	2.83
Total indirect expenses	48.28	53.76	59.23	64.71	70.19	75.66	81.14
PBDT	24.55	7.03	25.00	79.98	157.95	180.92	170.25
Depreciation and pre-op expenses	18.67	18.67	18.67	18.67	18.67	18.67	18.67
PBIT	11.08	–6.44	11.53	66.51	144.48	167.45	156.78
Interest	10.55	8.86	7.17	5.49	3.80	2.11	0.42
PROFIT BEFORE TAX	0.53	-15.30	4.36	61.02	140.68	165.34	156.36
Tax (Est. 35%)	0.19	—	1.53	21.36	49.24	57.87	54.73
PROFIT AFTER TAX	0.34	—	2.83	39.66	91.44	107.47	101.63
PAT to Gross income ratio (%)	0.2	—	1.3	13.3	22.4	23.1	20.9
Royalty & management fee as % of PAT	2081.3	—	455.3	39.8	20.4	20.0	24.0
ROI (%)	0.2	—	1.7	23.8	54.8	64.4	60.9

see arrangement that AHLL cannot afford to ignore if it wants to gain credibility to get in more trustworthy and competent franchisees. The question is: What should AHLL do about such an accumulated loss? Should it leave it to the franchisees to make up from future earnings and wipe off the accumulated loss? Or should AHLL bear the net loss as "investment" in the relationship? These questions have their answers in the domain of the choice between outsourcing and doing the work in-house.

Evidently, if AHLL were to expand on their own through wholly-owned subsidiaries (WOS), the fixed costs will be higher than if the franchisee were to put up the installations for them. Research has proven that this is mainly due to better local contacts of the franchisee for acquiring labour and better knowledge of local real estate. So much so, that the correct attitude of any franchisor should be to treat the initial losses—the genuine ones—as investment rather than as a responsibility of the franchisee. The argument behind this view is that had AHLL attempted to expand on its own, (a) the accumulated losses before breaking even would have been much larger (Figures D (i) and (ii); and (b) the time taken for breaking-even would have been longer (Figures E (i) & (ii)). If AHLL can assure this handholding in the initial phase of the franchisee arrangement, the existing franchisees will prove to be its major source of publicity and hence the catalyst to AHLL's further expansion in other regions.

Initial license fee and royalty: These two aspects of any franchise-arrangement send a powerful signal to the franchisees about the franchisor's commitment to the relationship and business:

a) The initial license fee of Rs 20 lakh appears to be on a very high side. AHLL may have its own cost-calculations. Nevertheless, such a high initial fee conveys that AHLL is trying to secure its position against a

Figure D(i)

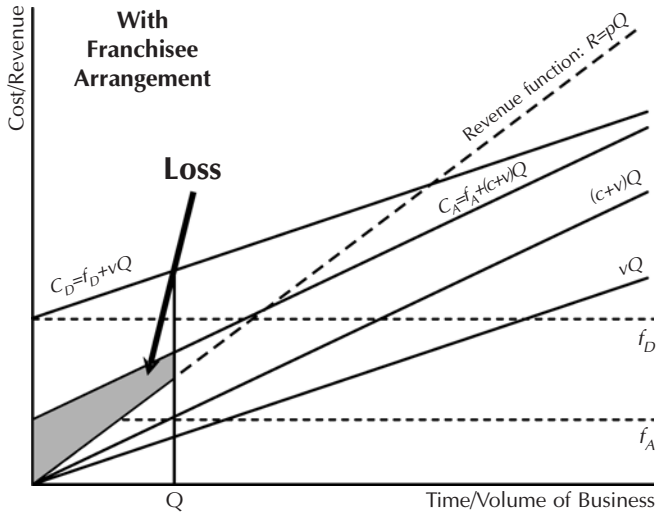


Figure D(ii)

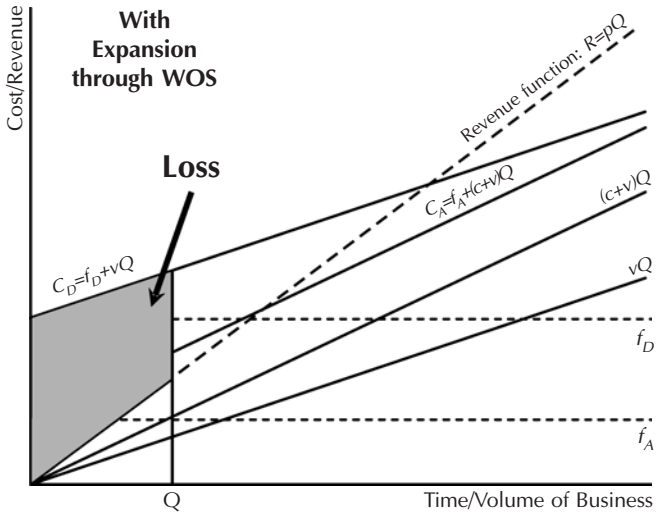


Figure E(i)

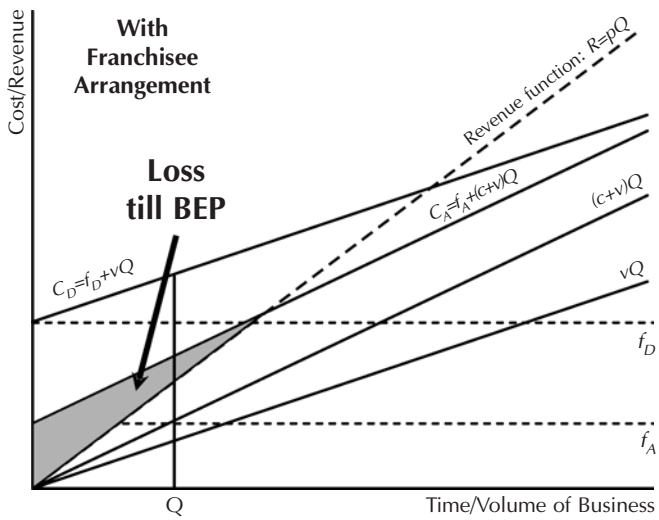
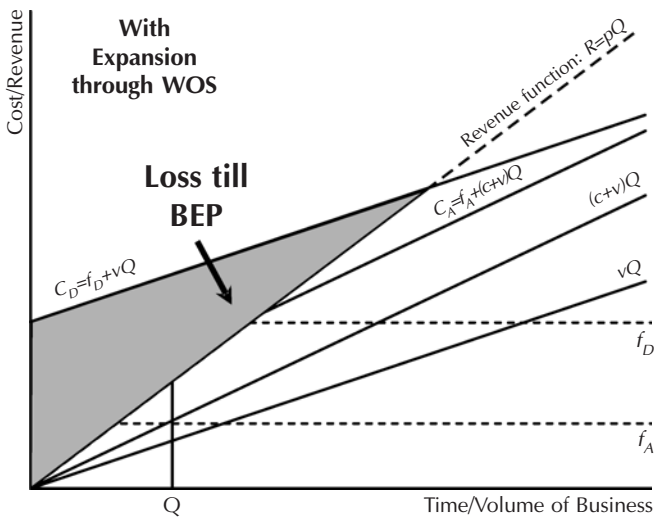


Figure E(ii)



possible business loss and pass on all business-risk to the franchiser. Though some franchisees may engage in the franchise with AHLL, the lack of trust emerges too early in the relationship and therefore in many cases, the franchise itself may be a non-starter.

b) The royalty rate is calculated on the gross income. On the surface, 5 per cent appears nominal. However, if we carefully look at Table A, it appears stupendous in the first three years. This raises the basic question as to whether AHLL is committed to the franchisee's profitability at all. If AHLL wishes to gain the confidence of the franchisee—and thus expand distribution/reach in other areas—the more appropriate sharing method would have been the PBT. This sharing could have been fixed at anywhere between 20 per cent and 35 per cent as deemed fit by AHLL. The current practice of 5 per cent on gross income implies that AHLL secures its royalty irrespective of the franchisee's profitability—a clear signal of lack of commitment to the relationship.

***Technical support*:** The Case also leaves the reader to wonder whether AHLL is able to—and really willing to—provide technical support in the form of Apollo's doctors making visits to the clinics from time to time. Such visits will certainly lend credibility to the franchisee and it will even improve the morale of the employees

such as technical support staff, nurses, etc. However, the letter from a franchisee (shown in a Box in the Case) causes much doubt about the execution of this aspect. From the letter, it appears that the only visits by Apollo's technical personnel are meant to "monitor" the activities of the franchisee rather than support their functioning for improvement. This clearly shows that AHLL is functioning on the basis of mistrust about the integrity of the franchisee and do not add any value to improve competence in delivering quality-service. One must be cautious in this regard as the Case provides only one such letter from a franchisee; whether this can be taken as a prevalent phenomenon is uncertain. However, even the mention about the franchisee being non-co-operative in reporting, training etc., indirectly points towards the weakness of the AHLL systems.

***Monitoring*:** The Case points out that the aggrieved franchisees engage in possible opportunism. However, the empanelled doctors of the clinic complain of poor patient-inflow. The fact that the clinic is competing with Max Healthcare in the vicinity, makes it important for AHLL to focus on competition and help this franchisee more effectively. However, one gets the impression that AHLL is merely blaming the franchisee for all the problems. No doubt, there were technical and teething problems in the beginning, which is to be expected in every budding relationship. That the problems were allowed to grow cannot be attributed to the franchisee alone. Interestingly, Mr. Jalan's suspicion that the franchisee may be collecting money from the patients without registering it through the software is an additional indication that monitoring of the franchisee's functioning is quite weak. Given the fact that the franchisees are likely to be widely spread across different towns/cities, monitoring from a single centralized location could be complex and less effective.

Marketing communication: AHLL strives to position itself as a *one stop value-for-money primary healthcare facility*. While this is both appropriate and laudable, the advertisement, when viewed critically, falls short of expecta-tions. Consider the following:

- ***"Life must be good" campaign:*** This advertisement is ordinary in its appearance and the picture can be confused with a plethora of advertisements for products and services ranging from sunflower oil, life insurance policies, home loans, etc. The first impression of this advertisement does not motivate one to give it a serious reading. It is likely to be lost among a myriad of advertisements that appear and disappear in print and electronic media. Besides, it does not convey the positioning message at first glance.
- ***"And you thought we're expensive" campaign:*** The advertisement does not bring out what the core service offered by AHLL is. It looks like an advertisement for a diagnostic laboratory services. This campaign, which otherwise is catchy, loses track of the core message.

What Needs to be Done?

- AHLL should handhold franchisees until a certain threshold level of clientele is established. The picture emerging from Table A warrants that this should be done at least for the initial two years. This handholding is to be treated as an investment in its business in the long run. This will reduce investment by that amount and will improve ROI.
- Initial license fee should be reduced to Rs 10 lakh, an amount that looks more reasonable. In addition, royalty should be pegged to PBT and not to the gross income, and it can be in the range of 20-30 per cent. This will improve the credibility of AHLL's faith in the franchise arrangements and its own commitment to the relations.
- AHLL should get a policy directive from the founder of Apollo Hospitals by which senior doctors are deputed to different AHLL clinics to share their knowledge. These doctors need not always be super specialists. Alternatively, the consultant doctors of AHLL's franchisees can be taken to seminars organized by Apollo Hospitals to share the latest knowledge in different fields of medicine. This will go a long way in building up a sense of belonging among the doctors who work with AHLL's franchisees.
- AHLL should employ an executive in every region where franchisees are located to regularly inspect the accounting matters. Since there is a lot of suspicion about the franchisee's opportunism, such close monitoring can prevent misreporting by franchisees. Besides, the executives themselves need to be rotated across regions to prevent their collusion with the franchisees over a period of time.
- AHLL should confine to the *'And you thought we're expensive'* campaign. This campaign is genuinely good. It catches attention since it talks about the cost;

the phrase "you" relates to the reader instantly. The caption challenges the reader and hence the chances of this advertisement being noticed are far higher. Moreover, it directly touches the heart of the positioning theme. AHLL will be better-off confining itself to this campaign alone, instead of wasting its efforts in the other campaigns. There is, however, certain scope for improvement. The copy has to highlight the central theme of the campaign, namely, primary healthcare service. It is not clear that the adverti- sement is focusing on primary healthcare, more importantly, preventive medicine. The subtitle can say, '*Preventive healthcare that fits your pocket, now at your arm's length.*' The title and subtitle can together convey most of the crucial message in this manner.

AHLL should use more "inclusive" practice for their franchisee-selection. When they sow more seeds over wider area, the chances of more franchisees succeeding are brighter. Apollo, like any brand-owner, has been bogged down with the fear of brand-dilution. It is highly improbable that brand-dilution will happen in primary and preventive healthcare where the treatment-failures are less likely. Hence, AHLL should try expanding vigorously, trying to reach about 500 franchisees so that ultimately the targeted 250 may actually germinate and grow.

Case Analysis III

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Problem Definition

This is an instance of an excellent marketing idea going down the drain because of bad implementation and wrong understanding of what is meant by 'franchising'. Mr Ratan Jalan has to decide very soon whether to continue with the franchising route or go ahead with the company-owned operations. Does it warrant a repositioning of the brand or a change in the brand itself? These were the key issues to be decided by him for the future of AHLL.

What prompted him to think along these lines?

- Even after six years in business, the company was making a revenue of just Rs 5-crore with marginal profits.
- Franchisees were unhappy with the kind of support and handholding they were getting from AHLL.
- Although the 'Apollo Clinic' brand was developed as a value brand with significant marketing efforts by the company distinctly different from the Apollo Hospital's premium image, the public perception was still of an upmarket brand having a 'not for everyone' image as per the AC Nielsen study.
- Franchisees were increasingly getting disenchanted with the Apollo Clinic brand, many of them being unwilling to renew licenses or maintain relations with AHLL as evidenced by the letter from the Delhi franchisee.

Alternatives

- Continue with the present arrangement and ensure that the clinics become viable
- Take over the sick clinics, revive them, and then hand over to new franchisees
- Establish and position a new brand with a scaled down image, disassociating itself from the Apollo brand
- Wind up the franchising business.

Analysis

Financials

The disenchantment of the franchisee arrangement stems from the core understanding of 'branding' and 'brand value.' Somewhere a mismatch of expectations between AHLL and the franchisees about how much the brand is worth is disturbing the cost-benefit equation for both of them. AHLL obviously thinks that the Apollo Clinic brand is worth Rs 20 lakh as a one-time licensing fee and considers the 5 per cent charge on revenue as an

annual fee, payable quarterly, as fair. The franchisees expect that the Apollo brand name would automatically get the patients in and they would be able to run a profitable operation right from the start. Unfortunately, in the service industry, more so in the healthcare industry, it is not enough to have a top class product; it must be always backed by a top class service. Service means different things to different people. In this case, every customer (patient) would view the brand based on hearsay or word of mouth and his/her last experience. Given that such experiences (moments of truth) are going to be few and far between, there is no scope for any lapses by the franchisee, whatever be the reason. Customers are not likely to forget such lapses, especially in case of healthcare. It is therefore important that both AHLL and the franchisee are in sync with what constitutes 'excellent service' in this industry, analyse the gaps, and plug the loopholes as far as possible. By merely giving an initial training and induction and handing over a Development and Operations manual to the new clinic staff, AHLL cannot completely absolve itself from the responsibility of ensuring that the franchisee operates at a profitable level. In my view, it is imperative that AHLL must ensure that the franchisee is able to hold its head above water at the initial stages. Otherwise, disillusionment is likely to set in and spread rapidly, thereafter.

Realistic Projections

A look at the projected P&L statements given to potential franchisees seems to be very optimistic in the estimates of business in the various categories. In the first year itself, the estimates are such that there is a break-even at a level of just below Rs 40,000 per day (Exhibit 1), whereas, going by the information given for the Delhi clinics, the actual figures are working out to be a little over Rs 20,000 taking 365 working days, almost half of the break-even. So, obviously, the estimates of revenue projected for the various categories such as consultations, pharmacy, walk-ins, diagnostics, and services seem to be rather optimistic. If this is happening in Delhi, figures for other smaller cities are likely to be even lesser. If the projected top line figure is not being achieved, then the franchisee is going to cut expenses to preserve the bottom line. Obviously, this would reflect adversely in quality and service. A more realistic picture could be given with slightly more conservative estimates of revenue and a projection of a loss for the first two years before profits are made. This would temper down the expectations of the franchisee and perhaps also reduce the number of applications for franchises , with concomitant saving of time for short-listing the prospective candidates.

Selection of Franchisees and Service Orientation

The criteria for franchisee selection seem to be inappropriate. In such businesses, having a service orientation is a must; albeit assessing those who have a service orientation could pose problems. Mere background, entrepreneurial interests, and financial strength of parties are not sufficient to succeed in this business. This is precisely why there are such high expectations for this business to be a sure success because of the Apollo brand name, which Mr Jalan refers to as the 'rent-seeking behaviour,' and disillusionment, thereafter, when it does not happen. Ideally, the person best suited for this franchising operation should be a person with a medical background and a service business orientation. Unless the culture of service is inculcated and practised from

Exhibit 1: Calculations to Show Break-evens as per the Estimates given in the Case

Break-even as per the projected estimate (143.49 – 0.54/12*30)	**Rs 39,703**
Revenue/day	
Consultations 30 * 200	Rs 6,000
Pharmacy @ 80% of 30 *125	Rs 3,000
Walk-ins (assumed at 20% of consultations, ie., 6*4*200	Rs 4,800
Diagnostics (assuming a factor of 3 200 *4)	Rs 2,400
*Services (assuming a factor of 3*200*8)	Rs 4,800
Total	**Rs 21,000**
Total annual revenue (taking 365 days of working)	**Rs 76.65 lakh**

* Actually this factor has been taken optimistically as compared to the data given in the Case. For smaller towns, it could be much lower, further reducing the annual turnover.

the top, it becomes very difficult to maintain this culture as the organization grows. In a franchising operation, except the internist, all other doctors are empanelled and are not on the rolls. It becomes extremely difficult to maintain a consistent culture, since the doctors practice at different locations, hail from different work cultures, and are strictly not under the control of the franchisee.

Viability of the Business

Mr Jalan is facing the apprehensions of a lot of franchisees who want to give up their franchise or refuse to renew their license. This can be fatal for the brand as well as for the future of the business as it is very difficult to find trustworthy franchisees. Yet he cannot display his desperation and yield to their terms. In my view, it is important for Mr Jalan that the current franchisees continue and renew their licenses for future propagation of the brand. Since most of the problems are stemming from the unviable volumes of business, perhaps a relook at the financial projections could help; and the 5 per cent royalty payments every year should be levied only after a floor turnover is achieved. However, safeguards have to be instituted so that the franchisees can register their turnover, bypassing the CMS.

Branding and Brand Image

While benefiting from the Apollo Hospitals association, the 'Apollo Clinic' brand had to also contend with the high price perception and an upmarket image, which it did not intend to have. Therefore, it is probably wise for the Apollo Clinic to now seriously think of disassociating itself from the Apollo brand name and reposition as a 'value' brand, which was its primary objective.. This requires major deliberation with the promoter because it would entail a slew of new marketing initiatives in establishing a new brand in the market. Though it is fraught with risks, it also stands to gain in the long term should the public view it positively. Given that the revenues are nothing to write home about, this is not much of a risk, if the business is to continue.

Segmentation Strategy

The concept of franchising is basically sound. In a Rs 100,000 crore industry, it would be impossible for AHLL to go about establishing its own healthcare units. However, if the basics of the revenue model for the franchising operation is tweaked and the right segments are tapped, this can still be a money spinner for the group. Benchmarking prices to some of the leading service providers in the city and then extracting a premium, perhaps is not a good idea. What is important is that prices should be benchmarked to a type of customer (patient) segment, and then if the volumes are viable, a city should be included to open an Apollo Clinic. Otherwise the break-even figures would be different for different cities and franchisees would be keen to cut corners to make up the numbers and show profit. Maintaining quality consistency would be key to the overall brand growth of 'Apollo Clinic'. Therefore, unless the choice of 'right' franchisees is made, quality and service standards are maintained, and a 'right' pricing is done, the task is difficult.

Morale Building

Mr Jalan has an immediate problem of stemming the flow of applications from the existing clinics that are either unwilling to renew licenses or want to close shop. The news of closure of the clinics could be disastrous for the morale of other clinics — not only for the ones that are struggling but even for those that are doing well. While there would be genuine cases where clinics might have to close down, this should be downplayed as far as possible. Resisting closure could be suicidal. Success stories of clinics should be prominently disseminated in appropriate forums and media, where the other strugglers could take a tip or two. AHLL stands to gain from clinics remaining in operation.

Recommendations

Therefore, if I were Mr Jalan, I would take the following decisions:

- Accept all requests for non-renewal of licenses.
- Close down unviable clinics and take over all viable clinics and run it temporarily, till a new franchisee is identified.
- Strengthen selection procedures to find the 'right' kind of franchisees.
- Establish a new brand for the 'Apollo Clinic,' disassociating itself from the Apollo lineage, yet maintaining the group identity and its intention to be a 'value' brand for aspiring middle class customers.
- Project more realistic estimates of business operations to reduce expectations and have only genuine and committed potential franchisees apply for such clinics.

- Educate the franchisees about the need to maintain brand consistency and image, translated into service quality and standards.
- Have a more proactive relationship with all franchisees and not leave them in the lurch in their hour of need.
- Deliver value for licensing and royalty fees charged in terms of counselling, handholding, and marketing the brand.
- Market preventive healthcare packages nationally to supplement the marketing activities of the local Apollo Clinics.
- Institute the 5 per cent royalty payment only after a floor revenue (to be decided by AHLL) is crossed, to ensure clinic viability.

Case Analysis IV

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One of the most challenging issues in service management is managing the distribution function. Service management entails three intricately-linked issues: service operations management, service marketing management, and service provider management. The core problem in all these three issues is service variability, also called service heterogeneity. This heterogeneity is contributed to as much by employees as by the customers themselves, being co-producers of the service. The challenge of distribution is that a highly variable service is less likely to be distributed.

However, variability of a service can be used to customize the service as per the requirement of the customer and can lead to higher satisfaction. However, this will essentially mean more employee empowerment and can lead to problems especially if the employee is a franchisee. This is because it will lead to a variation of costs as well as inconsistent branding. An additional disadvantage to the franchisor would be caused by the powerful franchisees who are difficult to manage. In service organizations, this is manifested by powerful employees who are often more important than the organization itself!

Apollo Hospital's venture into Apollo clinics has to be seen in this light. The key issue to be noted is that Apollo wants to keep the brand identity of the Hospital and the Clinic different, perhaps to communicate different value propositions from each of them. Therefore, Mr. Chokalingam's view on the letter from the disgruntled franchisee is correct. A franchisee has to follow the business model proposed by the franchisor. However the question is: Can the business model be standardized?

If one looks at the comments made by Mr. Jalan and Mr. Behl, there seems to be an essential contradiction between the core service offerings by the clinic and the way they wish to structure the same. Any service can be positioned on two dimensions—Divergence (the amount of freedom allowed to the service provider) and Complexity (the number of pre-defined steps taken to provide the service). For example, a pop singer is high on diversity but low on complexity, while McDonald is high on complexity and low on divergence. A service high on divergence is difficult to standardize. General Practitioners (GP) are high on divergence as they can provide base consultancy on a number of diseases. Hence, the essential contradiction. Clinics cannot compete with GPs and yet be under the control of Apollo Hospital.

So, based on the above discussion, I have the following to suggest:

Reduce total number of service offerings: I have a feeling that Apollo clinics are trying to do too much. The services should be restricted to those which can be standardized leading to a reduction in divergence. At present diagnostic, pharmacy, and consulting services are being offered. However, if consulting is left out of it, the other two are best suited for standardization. If the diagnostic services are focused on and the standards certified by Apollo Hospital, I think, the clinics can widen

their base. I guess (though it is not stated explicitly), the current referrals to both the diagnostic as well as pharmacy services are from the inhouse doctors. By removing consultancy, other GPs can also be induced to refer patients for diagnostic and pharmacy services and thereby increase turnover.

Invest in IT: Cases beyond the capabilities of the GPs can be referred to Apollo Hospital via the net and advice from the doctors in the main hospital can be sought. This will be of real value to patients, who need not travel to the Hospital for the pre-treatment process. This will in turn reduce the load on the main hospital.

Finally, it is important to understand that not all services can be standardized, nor is it desirable to do so!

Case Analysis V

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Issues to Address

The CEO of AHLL is examining the suitability of the franchise model for the business. The problem of AHLL is possibly not so much about the suitability of the franchise model as it is of estimation of the potential and the effort required for promoting the concept. The average royalty that a franchisee pays to AHLL, projected over year 1 to year 7, is Rs 15.77 lakh (Exhibit 5 of the Case). The projected revenue of AHLL from royalty paid by 50 franchisees is Rs 7.89 crore. As 50 franchisees are appointed over six years, it is assumed that every year, about 8 franchisees are appointed. The yearly revenue from license fee of eight franchisees is Rs 1.6 crore. As the total revenue for AHLL is given in the case as Rs 5 crore, the revenue from royalty is not more than Rs 3.4 crore a year. AHLL's revenue from royalty is 48 per cent of the projected revenue of Rs 7.89 crore. As royalty paid to AHLL is a fixed percentage of franchisee revenue, the revenue of the franchisee is also less than half of their projected revenue. The interest level of existing franchisees and the willingness to invest by businessmen/entrepreneurs is low as the earnings are substantially lower than the projected revenue. As returns are not as expected, the fault can possibly be that of estimation or of strategy or possibly both.

There are a few independent one-stop shop clinics available in certain cities. It is observed that the doctors empanelled in these clinics do not get sufficient number of patients. The interest level of the doctors is therefore low. The attendance of some of these specialists is irregular which in turn affects the flow of customers. These clinics slowly evolve into diagnostic centres even though they continue to offer consulting by specialists and also preventive healthcare check-ups. The concept of regular visits to these clinics does not exist; one visits only in case of an ailment. These clinics did not succeed in promoting the concept of preventive healthcare. Clearly, it is important to educate consumers for these businesses to succeed; and, therefore, the effort of Apollo Clinics in this direction needs to be examined.

Consumer Behaviour by Location

Preventive healthcare is a new concept in India and the willingness to accept a new concept could vary among different types of consumers. A long time resident of a town has knowledge of specialist doctors in the town. The consumer prefers to use this knowledge while selecting a doctor rather than relying on a particular brand. In the case of healthcare, ambience, convenience, and one-stop shop may not provide the relative advantage over trust in consulting. The labs and pharmacies in many small towns are located near hospitals and locations where well-known doctors have their practice. The consumer in a small town does not see an advantage in the Apollo Clinic unless he is made to realize the need for preventive healthcare. This requires a change in their mindset. In large cities, the floating population and the non-locals without much information about specialist doctors of the city, are possibly the consumers who perceive quality healthcare in the offerings by Apollo Clinic.

These consumers may visit for consulting at the time of ailments and for using other facilities, such as diagnostics or purchasing medicines rather than finding out about other outside service providers. The one-stop shop may have relevance for these consumers. These are also the consumers who are possibly willing to accept innovations and are therefore ready to switch to preventive healthcare earlier than the small town consumers.

Communication Effectiveness of AHLL

The existing approach of AHLL relies largely on word-of-mouth communication and less on paid advertising. AHLL does not want the Apollo Clinics to be perceived as an overly commercialized business proposition. The downside of this is that the new concept of preventive healthcare is not communicated to consumers. The type of effort required to educate the consumers is possibly not put in by AHLL or its franchisees. The franchisee expects the customers to walk in because of Apollo's brand name which seems unlikely. The insufficient effort is reflected in the average expenditure of Rs 12.47 lakh on marketing and sales promotion by the franchisee. Also, it appears that the projected marketing and sales promotion expenditure is worked out using a percentage of sales approach, as promotion expenditure is expected to be Rs 9 lakh in the first year and Rs 15.94 lakh in the seventh year. Clearly, this is not a promotion strategy for educating the consumer on the new concept. The education on a new concept requires a higher initial expenditure which can reduce over time for maintenance advertising. Thus it is not only that the franchisee is "reluctant to get his hands dirty" but in fact even AHLL does not expect the franchisee to develop the market by educating consumers on the concept. In the absence of such efforts by the franchisee, brand building and concept education have to be tackled by AHLL. At present, however, the investment by AHLL for this purpose is low. It appears to be a problem of lack of communication effort rather than of the franchisee model.

The franchisee model of healthcare can be found in some of the Health Maintenance Organizations (HMO) in the US. These organizations focus on corporate customers and persuade them to provide healthcare to employees through the HMOs. The Apollo Clinics also promote to corporate customers but it is not clear if the effort is to get the corporate customers to go for one-off health check-up or to get them to provide regular healthcare for the employees through these Clinics. The pricing differs for the treatment of corporate employees and it is not clear if any tariff arrangement exists as the same is not mentioned in the case. The corporate customers will find it easy to tie-up with a branded clinic and therefore this option has merit.

Service Delivery and the Franchise Model

The franchise model is advantageous as it allows AHLL to reach a large number of locations with limited investment. For this model to succeed, it is necessary that the franchisee finds the business viable. Initial analysis indicates that the actual revenue is less than what is projected. The performance may not be uniform and may vary between franchisees. It is influenced not only by the efforts of the franchisee but also by the nature of the market in which the franchisee operates. The understanding of the consumers described earlier suggests that the acceptance of the AHLL service by consumers is likely to be better in larger cities. Thus the franchisee would possibly find the business to be attractive in these cities instead of small towns. The larger potential in the cities also justifies having more than one franchisee as in the case of Mumbai. It also increases the efficiency of advertising expenditure which is important as promotion of a concept requires huge investment. It should in fact be shared by AHLL and the franchisee. In the initial stages, promotion should be treated as a deferred expenditure by both parties.

The effort required in smaller towns is greater than that in cities and the time taken for acceptance is also higher. The willingness of a franchisee to invest in such markets may not be very high where a sustained effort in educating the consumers on the concept is required for a longer duration than in the larger cities. AHLL may set up a few of its clinics at locations which are unlikely to be profitable in the short term but hold potential in the long term. This is an effort at market development and to demonstrate the presence of market potential in these places and thus create interest among entrepreneurs to take up the franchise. Setting up its own outlets would help understand the business better because of direct contact with the customers for service delivery. AHLL will be more sensitive to customers' and franchisees' needs and will also have a better control on the franchisees because of the knowledge of service delivery and its commitment to the concept.

Identifying the cities and towns to establish Apollo Clinics requires attention. An important strength is the Apollo brand name. The clinics are also expected to feed the Apollo hospitals with clients. This would suggest that the clinics be set up in locations where Apollo Hospitals are present. This, however, has not been observed as there are no Apollo Clinics in Chennai, Madurai, Hyderabad, and Pune. In addition to this, the composition of population in the larger cities and smaller towns differs and as indicated earlier, this is likely to influence the acceptance of the clinic concept and the brand. This also needs to be taken into account while deciding on the location for setting up an Apollo Clinic.

Sharing Responsibility for Promotion

Concept selling to change consumer behaviour is better achieved through personal contacts than through advertising. Personal selling effort is required particularly in the initial stage, say, for a year, and this can be handled by the franchisee. AHLL can develop a team of sales executives who are trained to educate the consumer on preventive healthcare. The members of team can be loaned to the franchisee for a fee. The franchisee may be required to take the services of the team for the first year as part of the agreement after which it can be left to him to decide. In the initial stages, it is advisable to have a trained sales team with AHLL instead of individual franchisees recruiting and training salespeople.

AHLL needs to invest in brand building for gaining confidence of the franchisees. The franchisee on establishing the business has loyal customers satisfied with the quality of service. He may then realize that the franchisor is not providing value for the royalty paid on a recurring basis. The customers who find the service to be good are possibly loyal to the clinic and a change in the brand name is unlikely to affect them as the service as well as the doctors remain the same. The franchisee may want a reduction in fee or a greater flexibility or even termination of the arrangement. This requires creating an association of Apollo Clinic brand with quality and innovation. In addition to promotion efforts, AHLL may need to bring the latest in the medical field and provide support to the doctors in the clinic. It would also need to keep innovating in service delivery so that the franchisees find it worthwhile to have a continued association with them.

If you take care of the small things, the big things take care of themselves. You can gain more control over your life by paying closer attention to the little things.

— Emily Dickinson