

## Article 1



## Features

**JOINING A CHAIN GANG**

Peter Switzer

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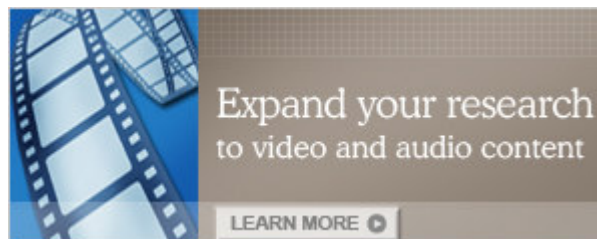
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## COVER STORY

Franchising is expected to become more popular as people lose jobs in the downturn, Peter Switzer writes

WITH the Australian economy heading for an economic slowdown at best and a recession at worst, two things are for certain -- some businesses will experience tough times and hundreds of thousands of workers will lose their jobs.

History shows that when some employees lose their jobs and are given a golden handshake, or are in an older age group where bosses often aren't focused, there is a tendency for the displaced workers to buy themselves a job by purchasing a franchise.

So what does someone need to know about franchising in a slowing economy? And which businesses are expected to do well, and which not?

``In the current economic environment the franchise systems that will perform best have more to do with the quality of the franchisor and underlying franchise system and business than it does any specific industry factors," says Adrian McFedries, of franchising consultancy DC Strategies.

``The franchisors best placed to perform well over the next couple of years are those that have the quality of infrastructure, people and capital, and continue to focus on the relevance of the franchise system, underlying business economics and the compelling offer to the consumer."

McFedries says more than 70 per cent of franchise systems have fewer than 10 operators, which is not a compelling reason to be in franchising. These franchises can succeed, but most cease to scale as the systems, structure and staff are insufficient to drive and sustain profitable growth.

Jason Gehrke of the Franchise Advisory Centre is another who chose to go with the strength in challenging times.

``Established systems with a critical mass of profitable, satisfied franchisees will not only weather the economic storm, they will come out the other side in top gear," he says. ``Quite possibly, many could buy out or take market share from a competitor or two along the way."

He was not inclined to name names, but points to salient characteristics of franchises he thought would do well.

``Cash businesses or those with incredibly tight credit controls combined with clever marketing and exceptional levels of customer service will do well," he advises.

``There are many examples of these in both service and retail franchise brands that fit the above criteria and will perform strongly in the next couple of years."

Gehrke says new franchise concepts emerge in Australia at the rate of about 100 per year, but like McFedries he suggests not all will be viable in the long term.

Concepts that maintain the functionality and extend the life cycle of existing assets do well in tough times when people cannot afford to buy new assets, he says. `` For example, home maintenance and renovation, vehicle rejuvenation and accessorisation help to extend the useful life of these assets when their owners can no longer afford to upgrade them for something new," he says.

`` Concepts, mostly mobile services franchises, that trade time for money by providing services, will still experience strong demand, as their customers are likely to be working longer hours in jobs where they will be expected to achieve more with less."

Katherine Sampson, an award-winning business owner, has been in her takeaway food business -- Healthy Habits -- for 16 years, but has only recently increased her franchising efforts. She has 28 outlets and 24 franchisees.

She has not been through a severe economic slowdown before. `` Our sales are down a bit and we haven't experienced the growth that we were expecting for the year," she admits.

`` However, the business, in a sense, is almost recession-proof, because we're in food, and people have to eat.

`` Secondly we're in the right space -- we're in the health industry."

Customers are cutting back on takeaway food, but they're not cutting it out altogether. Ironically, the threat of a recession might help, as rapid interest rate cuts may be a relief to some of her customers. `` Sales have suffered in areas where there are young couples with big mortgages," she says. `` We've got an area in Queensland suffering, we've got an area in Melbourne suffering -- wherever there's a new estate."

Sampson expects some interest in her franchises, given the prospect of future job losses.

She has not had any bites yet, but says history shows that during downturns, people start buying their own jobs through franchising.

**DC Strategy** research shows that the last time Australia had an economic slowdown, in the 1990s, there was in fact an increase in the number of franchisees entering the market.

`` The best indicator for the turning point has been the job index. It takes about nine to 12 months from the time it starts to drop for franchise inquiries to have a noticeable uplift," McFedries says.

`` In the current cycle that means sometime during mid-2009 we will see an increase in the number of people looking for franchisees."

He expects to see a couple of key differences in this slowdown compared with the 1990s. `` Firstly, since the 1990s there has been a dramatic increase in service, corporate and business-to-business franchise systems, so it will be interesting to view the statistics as to where people seek to invest in a franchise in the next 12 months," he says.

`` Secondly, the size of the secondary market for existing franchises relative to the 1990s is far greater and there will be a trend for more elderly, risk-averse investors to purchase existing operations rather than a greenfield operation."

McFedries says slower times mean some people do start to drop home services such as cleaning, but the rate hasn't been dramatic enough to affect the sale of lower-priced franchises.

`` In fact, during September and October a number of our clients experienced their busiest month in more than two years in the home services and food retail sectors," he says. `` Franchising has extended well beyond these examples, and groups such as ANZ Mobile Lending, Quest Apartments, Midas, Big Dad's Pies, Boost Juice, and PoolWerx -- to name a few -- have done well."

VIP Home Services, now with more than 1000 franchises, began in 1972, and has experienced a number of economic downturns.

``VIP has found that downturns in the economy increase the number of franchise inquiries and, in turn, sales," company founder Bill Vis says. ``This is because people are uncertain about their working future, so they want a stable employment position. What better way to secure your future than to be your own boss, work your own hours and earn a good living while doing it?"

Vis says a proportion of the population will be unaffected by the downturn.

``People are still on the same salary, are still time-poor and want to spend their leisure time with family and friends, not cleaning or gardening."

Buying a franchise is a serious business and should not be a stopgap to fill in for a lack of a job. Go with a proven system after doing a lot of research, contacting other franchisees in the system -- and working out if you are cut out for franchising.

That goes double when the economy is heading into an economic downturn.

#### RESEARCH IS CRUCIAL

EXPERTS say the key issues for franchisees do not change during tougher times.

However, they warn that it is necessary to be even more discerning.

Here are some key areas to focus on:

- \* The quality and relevance of the value proposition of the business to the end consumer.
- \* The quality of the infrastructure, planning, systems and people behind the franchisor.
- \* The detail in the franchise agreement and other legal documentation. Amazingly, there are still some franchisees who make the idiotic decision to wave independent advice.
- \* The perspective of existing franchisees who have been in the network for a while.
- \* The financial lending perspective; whether the bank has accredited the franchise system; and if so, what direction that accreditation has taken over the past year.
- \* The clarity and commitment of the management team -- this affects the performance and future growth of the business.
- \* Seek out independent experts on franchising who don't simply represent franchisors.
- \* Use a lawyer with extensive experience in franchising.
- \* Check out the information provided by the Australian Competition and Consumer Commission.
- \* Go to the Franchising Council of Australian website for information about franchising.
- \* And a word of warning: most franchises can be a rewarding experience and the dispute rates are low. However, many families have lost their homes and their wealth because they went into the wrong system at the wrong time, they were not cut out for long hours of work, they were not able to lead employees, or a shopping centre failed to deliver customers.

The R-word for franchising is not recession but research, and it has to be done. Jason Gehkre, of the Franchise Advisory Centre, tells us how much.

``As a rule of thumb, I would suggest that a first-time potential franchisee be prepared to spend about one hour of research for each \$1000 they are looking to invest in a business," he said.

``For a \$200,000 business, that's 200 hours of research, or five weeks' full-time work."

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