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Last week: DJIA 12273.26 ▲ 181.11 1.5% NASDAQ 2809.44 ▲ 1.4% NIKKEI 10605.65 ▲ 0.6% STOXX 600 287.99 ▲ 0.7% 10-YR TREASURY new, yield 3.644% OIL $85.58 ▼ $3.45 EURO $1.3547 YEN 83.47

FOCUS ON FRANCHISING

Industry Sees a Strong Rebound But Growth Will Be Uneven

By Julie Bennett

Franchising is expected to begin to bounce back this year, after a two-year slowdown. According to the 2011 "Franchise Business Economic Outlook," prepared for the Washington-based International Franchise Association by accounting firm PricewaterhouseCoopers, the U.S. franchise community will add over 19,000 new units and almost 200,000 new jobs.

Growth will be uneven, however, with sectors like automotive services, lodging and quick-serve restaurants expanding nicely, while franchises that offer services to other businesses will lag behind.

"One healthy sign is that capital is moving back into franchising," says Darrell Johnson, CEO of FRANdata in Arlington, Va., "because private equity firms are buying up franchise companies again." Catterton Partners of Greenwich, Conn., for example, purchased Noodles & Co., a 250-unit fast casual chain in Broomfield, Colo., in late December and Chanticleer Holdings of Charlotte, N.C. closed on the 452-unit Hooters chain in January.

But bank lending to franchisees remains tight. In the past decade it was enough for the franchisee to qualify for financing, Mr. Johnson says. Now franchise systems and franchiser performance also are being evaluated. "We are in a multiyear period of competition for loans," Mr. Johnson says. "Bankers are understandably more conservative early in the recovery and only franchise candidates that are the most appealing and franchise systems that can prove they are creditworthy will get funded."

Bypassing Banks

More franchise systems, like Snap-on Tools, in Kenosha, Wis., will continue to bypass banks altogether by offering financing themselves. Barrie Young, president of sales and franchising for Snap-on says, "We have provided in-house financing help to franchisee starts for two decades and have financed an average of 92% of new franchisees since 2007." In 2010, the 460-unit Lawn Doctor in Holmdel, N.J., helped to finance 10 of that system's 15 new franchisees, says Scott Frith, vice president of marketing and franchise development.

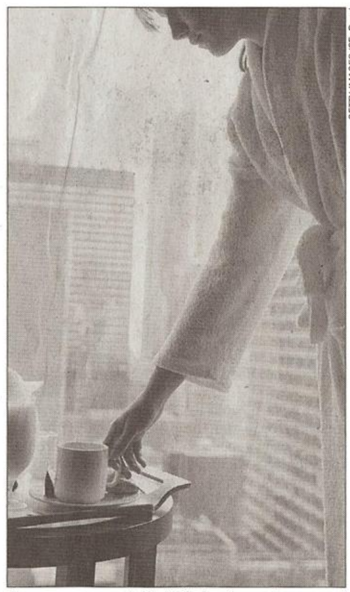
Much of 2011's expansion will come from existing franchisees adding more units, says Ron Feldman, CEO of Franchise America Finance, in Conshohocken, Pa., because banks are more comfortable lending to them. Phillip Patinkin, for example, has owned Auntie Anne's Pretzels franchises in the Chicago area since 1993 and recently added Red Mango frozen yogurt franchises to four of his 54 pretzel stores. "We have landlords asking us to open more Red Mango outlets," Mr. Patinkin says, "and we'll be able to, because we have a long-time relationship with our bank."

Dallas-based Red Mango opened 62 new franchises last year and will continue to expand, says James Franks, vice president of franchising, because the franchiser has adapted to the new economy. "Our total investment, of $262,000 to $400,000, lets new franchisees work out-of-pocket instead of borrowing money," he says, "and we're flexible about store size, allowing franchisees to open up in kiosks, malls, airports and college campuses or add them to existing franchised businesses."

Co-branding will be the expansion strategy for many restaurant franchise companies, including TRUFOODS, LLC the New York-based fast food franchiser of Pudgie's Famous Chicken, Wall Street Deli and Ritter's Frozen Custard and a master licensee and co-brand partner with Arthur Treacher's Fish & Chips. Says Gary Occhiogrosso, TRUFOODS's chief development officer: "The recession taught us to do more with less, and combining two or more of our brands maximizes rental space and allows franchisees to share resources, like walk-in refrigerators, bathrooms and employees." Central Islip, Long Island, franchisee Aman Singh says by co-branding Arthur Treacher's Fish & Chips and Pudgie's Famous Chicken he can offer more variety to his customers and increase the return on his investment.

Auto services franchiser Driven Brands Inc. of Charlotte, N.C., is looking over the nation's 5,000 shuttered car dealerships for future expansion, says Dave Schaefers, senior vice president of business development. Most are large enough to contain all three Driven brands—Meineke Car Care, Maaco Collision Repair and Auto Painting and Econo Lube N' Tune—and are already zoned for similar businesses, he says. After closing his Hummer dealership in Johnston, R.I., auto dealer Chris Hurd replaced it with Meineke and Thrifty Rent-a-Car franchises. Thrifty rents only used cars, so it works out well, Mr. Hurd says, to have Meineke mechanics nearby to keep them running.

The lodging industry is also on the mend, according to accounting firm Ernst & Young's new report "Global Hospitality Insights: Top Thoughts for 2011." Revenue per available U.S.



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Revenue per available U.S. hotel room is expected grow another 6% to 8% in 2011, and hotels in urban locations should fare even better.

hotel room increased 6% in 2010 from 2009, and should grow another 6% to 8% in 2011, the report predicts, as both individual and business travel pick up. Hotels in urban locations, like New York, Boston, Denver and Miami should fare even better. Choice Hotels International of Silver Spring, Md., franchiser of 6,000 hotels, with brands that include Comfort Inn, Quality Suites and Econo Lodge, added about 60 new hotels last year. By last month, Choice had already announced two new franchise deals for Cambria Suites in New York, and said that, as of Sept. 30, 2010, it had 540 more U.S. hotels in its pipeline.

Starwood Hotels (Sheraton, Westin, St. Regis, Aloft) in White Plains, N.Y., also has expansion plans, but 70% of its new hotels will open overseas. Starwood will open 70 to 80 hotels in 2011 and more than half of them will be in China, India and Thailand.

Interest in Asia will rise among many franchisers this year, says William Edwards, CEO of Edwards Global Services in Irvine, Calif., "because that's where the buyers are, and they want American brands." Unlike their U.S. counterparts, Asian franchise candidates typically have no financing problems, he says, and want to open U.S.-style education, restaurant and service businesses. Abrakadoodle, a children's art franchiser in Reston, Va., for example, now has franchisees in Japan, China, Malaysia and Singapore and several senior health care and handyman services have an Asian presence. YUM Brands, the Louisville, Ky., parent of KFC, Pizza Hut and Taco Bells, earns almost half of its profits from KFC stores in China. McDonald's, meanwhile, plans to have 1,000 restaurants in China by 2013.

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Social Networking

This year is also expected to see a rise in social media use. Scott Iversen, director of marketing for Toppers Pizza, a 28-franchise chain based in Whitewater, Wis., says that social networking is the best way to reach his chain's target market of 18-to-24-year-olds. Toppers has over 26,000 Facebook fans, Mr. Iversen says, and engages them with pizza recipe contests and weekly specials, plus a blog, a Twitter account and lots of videos on You Tube.

Franchisees are also experimenting with Groupon, the website that offers daily deals, but they should use caution, warns Erik Bostrom, a Hand & Stone Massage and Facial Spa franchisee in Highlands Ranch, Colo. "I offered a 50-minute hot stone massage for $35 on Groupon—the regular price for a non-member is $99.95—and had 1,288 people respond. Luckily, I have a massage facility with 10 rooms that's open 90 hours a week and could meet the demand." Social media, he says, is so powerful that it can quickly convey negative information about a business, too. "Can you imagine what would have happened if I couldn't have taken care of everyone," wonders Mr. Bostrom.