

SUCCESSFUL DELIVERY

Do you dream of owning a franchise but don't know which offer the best prospects? Jackie Pearson spent three months examining all available systems to ascertain the top eight.

Investing in a franchise is not an easy road to riches. For a start, there are 960 franchised brands to choose from in Australia. Some have proven track records and worldwide success. They're usually the ones that require a big initial investment and are extremely picky about who they'll accept as a franchisee.

Other franchisors are small business people themselves and have lesser-known brands. They require smaller outlays to start with but the risks are much higher. Some may well turn into tomorrow's big brands but others will never get off the ground. They could be bought out by other organisations or the brand simply may not work.

According to Franchise Council of Australia chief executive Richard Evans, one in five franchisees will not make it.

"It's more successful than marriage," Evans says. "And the thing about it is that both are relationship driven. To be successful in a marriage or a franchise takes good communication and a commitment to developing that relationship."

Australian Competition and Consumer Commission small business commissioner John Martin says Quiznos is a recent example of what can go wrong.

"The problem was a simple one and it was surprising because Quiznos was a copycat of another food brand that had set up in America as a franchise system and was doing pretty well," Martin says.

"The individuals involved initially started two corporate retail outlets in Melbourne and then made verbal promises to potential franchisees about the investment potential if they decided to get in early.

"Over 20 individuals paid the initial franchise fee of \$25,000 and then committed [to fitting out] their shop, which pushed it up to \$200,000. Some of the representations about what you could expect to make, some made orally at presentations, were not based on facts. By the time the ACCC got involved, most of the stores had closed and the business had gone into liquidation," he says.

The promoters initially offered undertakings enforceable in court, but during the negotiating process, it was discovered that they couldn't meet franchisees' claims for loss and damages. The franchisor, the ACCC and an independent third party negotiated a settlement and franchisees were refunded their initial fee.

Martin and Evans agree that the best way to minimise investment failure is to carry out substantial due diligence before investing. And that's where *AFR Smart Investor* can help. For the second year running, we've examined more than 600 franchisors, looked more closely at the offerings of a final field of 50 and come up with a shortlist of eight that we think make worthy investments.

And the winners are...

We've divided the winners into four categories, depending on how much capital is needed to buy in. The scores indicate how each franchisor performed in our assessment of the number of franchises available, company history, availability of trademarks, standards of training and support for franchisees, longevity of franchise agreements and exclusivity of business or marketing territories. See the table on page 44 for more information about each of our final eight.



THE WINNING FRANCHISES

If you have less than \$50,000 to invest	Scores (%)
Jim's Mowing	77
The Shed Company	51
If you have between \$50,000 and \$149,999 to invest	
Mr Carports	78
Contours	70
If you have between \$150,000 and \$299,999 to invest	
Domino's Pizza Enterprises (DMP)	83
Goodyear Autocare	82
If you have \$300,000 or more to invest	
Red Rooster	77
Fernwood Women's Health Club	70
Best overall performer:	DOMINO'S PIZZA ENTERPRISES

To come up with our recommendations, we had to make the tricky journey through franchise land, just like you would in order to conduct proper due diligence before parting with your money. Here's what we learned that might help you along your journey.

Dodge the dodgies

According to the ACCC's Martin, you're more likely to come across rogue operators at the bottom entry level, where you need between \$10,000 and \$50,000 to invest. Fortunately, we didn't detect any totally exploitative or rogue operators, but Martin says they do pop up from time to time.

"Usually, we get a bunch of complaints or inquiries about a system that's not a genuine franchise," Martin says. "They make claims that are just not sustainable about what the business will do. For instance, they say you will earn \$100,000 per year guaranteed or they provide no disclosure document. They don't have any substance behind them."

Martin says the ACCC tries to get in before people have parted with their money. It monitors advertisements and conducts outreach programs from its regional offices.

"It is a bit sad that people are still their own worst enemies and don't check out the validity of franchising systems," he says.

Are big brands best?

Most of our winning franchisors this year are well known, but high-profile brands are not always the best franchisors. Brian Rohan is founder and managing director of one of the lesser-known brands, Mr Carports. He and a partner started the franchise in the 1990s. The company sells and installs verandas, pergolas and decks, as well as carports.

"We did everything properly back in those early days and the business just grew and grew until we had to either employ more people or find another solution. We decided the best solution was to franchise," Rohan says.



CASE STUDY

Alita Ashcroft and Alexandra Shaw opened their first Contours Studio in Woonona, north of Wollongong, NSW, in October last year. They borrowed \$50,000 as an initial investment and also paid a \$5000 deposit for the option to take on a second women's gym site in Dapto, which they are due to open soon.

Proving that insider knowledge helps, Alita had worked for one of the founders of Contours since she was a teenager. She studied to be a physical education teacher but was then offered a franchise development position with Contours.

Alexandra worked as marketing and publicity manager for a local television station. It is the combination of Alita's company knowledge and Alexandra's local marketing expertise that has helped the partners develop their business.

When they set up shop, there was only one other local women's fitness centre.

"We're now within a five- to 10-kilometre radius of another four female gyms," Alita says. "But we're meeting our targets and at the moment we are one of the top five Contours franchisees in the country."

Alita attributes their success to working in the business as well as on it; focusing on local marketing strategies; following head office systems; and using a reliable accountant for financial advice.

NEED TO KNOW

- www.accc.gov.au now publishes franchising complaints, investigations and outcomes. It provides information about franchisors that have come to the regulator's attention. It also offers a good understanding of the types of difficulties and disputes that can arise between franchisee and franchisor.

NEED TO DO

- The Franchise Council of Australia website, www.franchise.org.au, includes a comprehensive directory of the systems available in Australia.
- Contact the ACCC to find out about its outreach programs conducted from regional offices. Visit www.accc.gov.au for more information.

	<\$50,000 initial capital investment		\$50,000 to \$149,999 initial capital investment	
				
BRAND NAME	Jim's Mowing	The Shed Company	Mr CARPORTS Outdoor Living Designs	Contours
Business type	Lawn and garden services	Prefabricated steel buildings	Verandas, pergolas and decks	Women's fitness studios
AFR Smart Investor score (%)	77	51	78	70
Initial capital investment (\$)	20,000	30,000	52,500	100,000
New franchise units available	Unlimited	30	18	208
System in operation since (year)	1989	2005	1997	2005
Estimated weekly franchise turnover (\$)	1442	From 13,460	4800	1540-11,540
Estimated weekly ongoing franchise fee or royalty (%)	From 77	Nil	288	200
Estimated weekly marketing fee (\$)	24	Nil	35	45
Estimated weekly training fee (\$)	17	Nil	Nil	Nil
Term of franchise agreement (years + options)	10 + unlimited 10-year options	5 + 5-year option	5 + two 5-year options	10 + 5-year option
Exclusive territory	Yes	Yes	Yes	Yes
Web address	www.jims.net	www.theshedcompany.com.au	www.mrcarpports.com.au	www.contours.net.au
Email address	jim@jims.net	jane@theshedcompany.com.au	br@mrcarpports.com.au	info@contours.net.au
Phone	131 546	07 5665 5666	08 8370 9523	1300 657 339

Now he is about to export the Mr Carpports brand to the United States.

"We're already opening our first branch in California. We also want another 10 branches in Sydney and four or five in Brisbane, and we expect to open in Perth when we find the right person."

Are you the right person?

Our research indicates that the best franchisors are those who will go to just as much trouble to find the right franchisee as you should to find the right system.

"The main thing that makes a good franchisee is a high degree of common sense," Rohan says.

"We get lots of people who want to buy franchises and you can tell when they ring up they just haven't got it. They ask stupid questions like 'How much money can I make?'"

Rohan believes that he could sell 100 Mr Carpports units, but he's more interested in the success of his existing franchisees and the ongoing development of the business and its system.

"A smart, intelligent person can buy a franchise very easily," he says.

Inside information

However, our research indicates it's easier to get into a sought-after franchise system if you have inside information. Two of our case studies - Nick Knight from Domino's Pizza Enterprises and Alita Ashcroft from Contours - both worked for their companies as employees before becoming franchisees.

Their experience as employees gave them an in-depth understanding of the system and procedures and their prospects for investment success.

Domino's national franchise operations manager, Adam Pratt, has been with the company for almost 20 years, having started as a driver in 1988. He worked his way through the system to franchisee level, ending up with stores in the ACT and Queensland.

"We had a very proactive and supportive franchisor who worked in conjunction with us as a business partner, rather than a policeman. Domino's worked with us, supported us, challenged us," Pratt says.

"It certainly helped to promote from within wherever possible. Internals know the business, the long hours, the challenges of working with a lot of younger team members.

"But we have had a lot of success with externals, particularly within the last couple of years. There is absolutely potential for externals. It's really very targeted where we're putting stores now.

"Our major focus for the next couple of years is to build our major markets in New Zealand and Sydney and large regional towns in NSW, Victoria, South Australia and Queensland."

The way in

If you don't want to work your way up from pizza delivery to successful franchisee, you'll need to go through a rigorous selection process if you want to invest in a robust, successful franchise.

At Domino's, the first part of the selection

process is a phone interview with the franchise recruitment manager.

"We explain that this is very much a hands-on business. We work very much in the stores.

"We do not expect franchisees to buy a store to sit at home in the lounge and watch it grow. Most of our stores are open 14 hours a day, seven days a week," Pratt says.

Applicants will need a minimum level of capital, which can vary depending on the location and the cost of fitting out the store. They'll then be asked to complete a full confidentiality form and a formal application form detailing all assets, liabilities, how much they're prepared to invest, work history and their reasons for wanting to be a franchisee.

An interview with Domino's national franchise team then follows. This focuses on operational issues, fast-food industry knowledge, and expertise in finance and business management.

If after all this you're deemed suitable, you'll be issued disclosure documents under the Franchising Code of Conduct, and it's at this point you will need independent legal and financial advice.

But that's not the end of the process. Next, you spend a few days in a store with a successful franchisee and are re-interviewed. After that, you'll be required to pay your franchise fee and undertake eight weeks of training, and even then you may have to wait for an appropriate site and for the store to be built.

"The whole process can take from 15 weeks to six months," Pratt says. "Generally, at the moment, about 1 per cent of inquiries make it through to franchisees. A lot of people are

\$150,000 to \$299,999 initial investment

>\$300,000 initial investment

**GOODYEAR
AUTOCARE**

Fast food

Tire and service centres

Fast food

Women's fitness studios

83

82

77

70

From 250,000

150,000

450,000

300,000-400,000

11

130

Unlimited

40

1988

1989

1979

1995

5000-40,000

11,500-115,000

Not provided

11,100-48,100

350-2800

nil

5pc weekly net sales

770-3370

300-2800

345-3450

6pc weekly net sales

550-2400

nil

nil

\$115

192

10 + 10-year option

5 + two 5-year options

10 + 10-year option

5 + 5-year option

Yes

Yes

No

Yes

www.dominos.com.au

www.goodyearautocare.com.au

www.redrooster.com.au

www.fernwoodfitness.com.au

franchise.enquiries@dominos.com.au

michael_middleditch@goodyear.com

tacey.steinmans@red-rooster.com.au

kel.balch@fernwoodfitness.com.au

07 3633 3333

01 8416 7408

07 3499 2100

03 9630 8800

competing for our stores and sites. Between 1 per cent and 2 per cent of our franchisees will fail and inevitably they're the ones who don't follow the system."

Be prepared to borrow

Pratt says it is essential for new franchisees to borrow money in order to purchase a store, so if you are serious about buying a franchise, make sure your credit history is in good shape.

Reputable franchisees such as Domino's will have accreditation with several or all of the major banks and this can certainly make it easier to secure the finance you need.

Of course, it is vital to make sure you will be able to meet interest payments and eventually repay the debt. This can be particularly difficult in the start-up period of any business.

Too good to be true?

Profit projections offered by the franchisors who responded to our survey ranged from a conservative 2 per cent a year through to 40 per cent a year. As with any investment, if it sounds too good to be true, it probably is. Always ask for projections in writing and don't believe them until you see it in black and white.

The more reputable franchisors are less inclined to provide any projections about future growth or franchisee turnover.

The best way to find out real earnings potential is to talk to existing franchisees. If a franchisor is not willing to give you the contact details of existing or previous franchisees, it can be a sure sign that they are inflating your earnings potential.

Likewise, ongoing fees and expenses range from nil to thousands of dollars a week.

Make sure you know exactly how those fees are calculated and feel confident about the services, marketing support and training you'll be getting in return.

The bottom line

Investing in a franchise is hard work and there's more to it than the initial amount of capital involved.

Many franchisors charge ongoing royalties and marketing fees, and some charge for training. You will have to pay rent, loan repayments, staff costs, stock, insurance, along with all the other costs business owners incur.

A good franchisor will offer excellent support, a proven system and procedures, and a marketable brand to underpin your business success. But your investment, particularly in local marketing and in being prepared to do hands-on work, will be ongoing.

"A lot of people who sign up for a franchise are retiring from the Defence Force or leaving professions like teaching," the ACCC's Martin says.

"They are pretty switched on and know about the job they used to do but they don't have a great deal of business acumen.

"They have this retirement payout burning a hole in their pocket, but we have a pretty saturated market at the moment.

"Be careful if the entry process is too simple. It's like the old Groucho Marx saying: 'It can't be much of a club if it would have me as a member.'" ❖

THE Si TEST

Step 1: We canvassed more than 600 of the franchised brands available in Australia. We then surveyed those franchisors who were members of the Franchise Council of Australia, were Australian based and had franchising opportunities available in at least three states.

Step 2: Respondents were scored based on:

- The number of franchise units they have available.
- The number of years they have been successfully operating as a franchisor.
- If the business involves the sale of a product, then that product had to be trademarked.
- No requirement for non-refundable payments apart from official franchise fee.
- No requirement to pay for supply of goods above wholesale or significantly discounted prices.
- Ongoing royalties, marketing and training fees.
- Terms of franchise deal, plus renewal options.
- Initial and ongoing training and support provided by the franchisor.
- Exclusivity of business and/or marketing territories.

Step 3: Based on data the franchisors provided, we estimated ongoing royalties, training and marketing costs on a weekly basis, as a percentage of turnover.

The two top-scoring franchisors from each initial capital investment category (less than \$50,000; \$50,000 to \$149,999; \$150,000 to \$299,999; \$300,000-plus) are included in our winners table on page 42, and inset.