

David or Goliath? Start-up or Established Franchise Concept

By

Peter M. Birkeland, Ph.D.

Let's face it: With over 3,000 different franchise concepts in over 100 industries, for most people it's a daunting task to select the right franchise for them. Seasoned franchise consultants would have you follow your passion in selecting a franchise, and while that's good advice to narrow down your choices to an industry or sector, it doesn't help much in choosing between several franchise companies in the same business.

One of the most significant decisions you'll have to make is whether to go with a start-up franchise or a mature concept. According to statistics by FRANData the median size of franchise systems is only 80 units—enough to be on a first-name basis with everyone, but hardly enough to have a critical mass for brand awareness. Even more telling, FRANData notes that about 7 percent of all franchise companies have as many as 1,000 units. In reality, most franchise systems are small.

What should you look at in evaluating start-up and experienced franchised concepts? What are the main differences and similarities? What impact does start-up or established franchise have on you and your profitability?

Risk versus Reward

There are at least two types of risk associated with buying a franchise and these risks differ based upon the maturity of the concept. One risk has to do with understanding the business model based upon historical performance. Mark Siebert, CEO of the iFranchise Group, put it this way. "In an established concept you have a track record to look at that will help you gauge risk. You'll be able to determine historical rates of return, historical litigation and generally know more about the company." Does this mean that a start-up is a bad investment? Not quite, as Siebert notes, "You should look to see whether a start-up is just providing a me-too concept, or whether they have built a better mousetrap. And if they are the first one in a new segment then you'll have the opportunity to own the marketplace."

Another risk factor has to do with the financial model attached to a start-up or established concept. Jeff Rosenfeld, Managing Director of Kessev Finance, suggests that there are pros and cons to both start-up and mature concepts.

"There is a lot of interest in start-up franchises because they're generally cheaper and there's more upside. But there are significant leverage points in a mature

concept that a start-up just doesn't have and can't get, like the ability to realize synergies in real estate, construction, or price breaks from vendors because of the sheer size of the chain. Also, it is easier to get financing if you're buying a well-known brand."

There is actually a third risk, or factor, that is very important and that has to do with the relationship between the franchisor and franchisees. For this perspective I turned to franchisees who are involved in various stages of franchising.

Franchisee Experience

Bob and Maurita Elias are seasoned franchisees who have owned two different franchises over the past ten years, but they are the very first franchisees of the Woodhouse Day Spa. "We weren't even really looking for a franchise," stated Maurita, "but we were looking for a change of direction in our lives. Our vision is about health and wellness and giving back to the community that has supported us so long. When we met with the founders of the Woodhouse Day Spa it resonated with us immediately."

Certainly as the very first franchisees there must have been a risk analysis that Bob and Maurita performed. "We didn't look at this from a purely intellectual point of view. It was from the gut. We really felt that the management team shared our values of honesty and integrity and from our past experience we know that is really important." In the case of Woodhouse Day Spa there was an added risk since the founder, Jeni Garrett, is a 25-year-old CEO.

But despite Garrett's age Maurita is impressed. "When she told me her age I was stunned because she is so intellectual and mature in terms of her business knowledge. She absolutely won't let anyone fail."

For John Francis, a PostNet Area Developer in Minnesota and Wisconsin, the decision process was based on potential. "Once you figure out that the business model works and that the people you're dealing with are good people, you need to figure out how things will work in your market. So even though PostNet is not a start-up, I was basically a start-up in trying to build the brand in Minnesota and Wisconsin."

What advice does Francis have for others in his situation? "I conducted a thorough market analysis. I looked at mature markets for this business and saw that they were still growing and that in my market we were about half the number of units for the same population, so I knew there was a lot of upside."

And since Francis is selling franchises, what does he tell prospective franchisees about his "start-up" in the upper Midwest? "Well, people always want to know the financials and we talk about that, but one of the things that I say is that we're truly

committed to the franchisee. We're in the franchise business and we take the franchisee seriously. Besides, this company is still small enough that you get a lot of attention from the senior management and staff. I can call up Steve, our CEO, at his home on a weekend and he'll take the call. That won't happen at the big companies."

So, after you figure out what you really want to do in franchising, and you narrow the choices down to a few select companies, look carefully at the risks and rewards of a start-up versus a mature. Perhaps most importantly, even the finance expert, Jeff Rosenfeld notes the importance of values and management integrity, "Probably the most important analysis is not the financial analysis but the people side. You need to be very, very, careful about the people on the franchisor side.

* * *

Peter Birkeland is an author, speaker, and management advisor based in Chicago. He conducts the [Franchise Boot Camp](#) around the United States to help people excel in franchising. To learn more about franchising and how you can be a successful franchisee, contact Peter at Peter@Franchisebootcamp.com or call him at 708-354-5534.