

Franchising on the rise in Australia

Abstract:

Tens of thousands of people across this nation are franchise owners, and for good reason. Franchises allow you to become a small business owner under the umbrella of an experienced business, with support from the company to bring new products and services to your neighbourhood. Low-cost franchise opportunities allow for unlimited growth, allowing financial freedom and the chance to achieve both personal and professional goals. Here will see the Rise on the Australian Franchises, Franchising Growth Sectors,

Introduction:

Franchises start with a growing company that has a trusted brand and is looking to expand into new communities. As they grow and streamline their business, they open their doors to others. Franchisees can start their own business with the support of the established brand, bringing jobs and economic growth to their communities. These franchise owners can support their families as well as give back to neighbourhood schools and organizations.

The sector is becoming increasingly active in trying to attract Gen Y as franchisees, with more than half of the franchisors using specific recruiting tools in a bid to attract this group, compared to only 38 per cent in 2010. An example is the Baker's Delight Fast Franchisee program aimed at bringing potential franchisees through the employee ranks – you can read more about this on page 12 within the report. Another key area for franchisors to look for new franchisees is, in fact, existing successful franchisees from within their network. The results tell us that on average, only 11 per cent of units are owned by multi-unit owners and that most franchisors believe they have another 15 per cent of their network who could become multi-unit owners. Whilst there are many franchisors who continue to question whether multi-unit ownership will just create more problems for them, it seems to us that many of the perceived issues can be overcome if franchisors adopt a specific strategy and approach to multi-unit ownership. In relation to funding, it is surprising that only 38 per cent of all franchisors (including just 33 per cent of the larger retail franchises) have their

systems accredited with banks – a staggering 75 per cent of smaller systems are not accredited. This is perhaps an indication of the difficult and timeconsuming accreditation process adopted by the banks, and also the fact that over the past few years, banks have been inconsistent in their approach to lending to the franchise sector. This presents a huge opportunity for a financier to ‘get it right’.



Figure 1

The franchising sector contributes an estimated \$90 billion per year (about 11%) to the Gross Domestic Product and employs over 600 000 people in Australia, a figure that between 2002 and 2004 increased by about fourteen percent and between 2004 and 2006 by about thirteen percent¹ Despite its importance to the national economy, there is little reliable evidence of the economic effectiveness of the operation of the sector. Franchising is portrayed by its trade association as a vehicle to transform inexperienced people into successful business owners, with higher success rates than for independent small business. The following quotes from the Franchising Council of Australia (the FCA) website give a sense of the ‘promise’ of franchising:

- There are countless benefits to becoming a Franchisee, which is why Franchising is one of the fastest-growing sectors of the Australian economy.
- The support and benefits provided by a Franchise system greatly reduce a Franchisee's business risks.

- It is also a Win-Win relationship where the franchisor is able to expand its market presence without eroding its own capital, and the franchisee gains through access to established business systems, at lower risk, for their own commercial advantage.

AUSTRALIAN FRANCHISING Growing or Not?

The 2016 Franchising Australia survey is the 10th in the series, which has been carried out every two years since 1998 by Griffith University's Asia-Pacific Centre for Franchising Excellence.

An Executive Summary issued by the Centre ahead of the full report says, 'Despite a relatively flat economy and retail environment, Australia's franchise sector continues to grow in total sales turnover and employment and its franchisors are confident of further growth in the next 12 months.'

The survey finds that the total annual sales revenue for Australia's entire franchise sector is estimated at \$146 billion, up from \$144 billion in the 2014 survey. However, this rise of 1.4 percent comes against a background of 2.5 percent inflation in y/e 2014 and 1.5 percent inflation in y/e 2015.

The total number of people directly employed in business format franchising in Australia has continued to rise with 472,000 permanent, part-time and casual employees, up 2.4 percent from 461,000 two years ago.

The number of franchise brands operating in Australia has declined by 3.5 percent from 1,160 to 1,120. Professor Lorelle Frazer, Director of the Centre, said this gradual reduction in franchise systems is expected as the sector continues to mature.

'Franchise brands have continued to merge and consolidate to remain sustainable and to grow,' she said. 'Whilst the number of brands has declined, individual franchise systems have grown internally with modest increases in the number of franchise units.'

The 2016 survey shows a total of 79,000 units operating in business format franchises in Australia. The number of franchised units has slightly increased and company-owned units decreased (perhaps as companies re-franchise outlets

they re-acquired following the GFC or franchise outlets they opened themselves through a lack of suitable franchisees). There has been no net overall change in the number of franchise units since the 2014 survey.

The survey notes that New Zealand remains the most common destination for Australian franchisors seeking to expand internationally, 'despite its small potential market'.

The proportion of franchisees in dispute with their franchisor across the sector was estimated at 1.8 percent, consistent with previous surveys. Disputes with franchisees involving an external advisor were reported by 25 percent of franchisors with a median of 2 of their franchisees. The most common causes of disputes were those related to franchisee compliance, communication issues and disputes regarding fees.

Bruce Billson, Executive Chairman of the Franchise Council of Australia, said franchising is a robust, vibrant and exciting part of the economy, accounting for approximately 4 percent of all small businesses in Australia.

'The survey results show Australia's franchising sector has continued to perform strongly, against the backdrop of relatively slow economic growth. The Franchising Australia 2016 survey points to a maturing sector holding its own in a transitioning economy following the end of the mining boom. Total sales turnover for the sector has risen slightly, while employment has steadily risen and created more permanent full-time jobs. Franchisors are also predicting growth in franchise numbers over the next 12 months.'

What's driving the franchise sector right now?

The franchising industry is still growing, despite being a mature sector. In the five years up to 2015-16 there is an expected annualised growth of 2.8 percent. In the five years through to 2020-21, growth will be a steady 2.3 percent. That will take the sector's franchisor revenue to \$192.6 bn.

Franchising has seen some ups and downs in trading conditions, and as it heads into the next five years consolidation of businesses is expected to create more multiple-brand franchisors. There will be more franchisees across their networks too, and a trend for these franchisees to operate more than one unit or outlet.

Perhaps surprisingly the growth from new businesses has come from retail-based operators entering the franchise arena.

Ambitious Generation Y who see franchising as a way to run a business with support and training have, with financial assistance from their parents, helped drive the sector on.



Figure 2

Corporate downsizing has also brought in new franchisees.

Looking ahead there is likely to be stronger demand for service-based franchise operations in line with social and demographic trends. Consumers will increasingly look to have some domestic chores outsourced as they are time-poor but with discretionary income. Gardening and cleaning, for instance.

Day spas and beauty salons are expected to continue their growth trajectory as consumers with spending power look to indulge in luxury goods and services.

And an ageing population adds its own dynamic to the spending pattern - a focus on healthier lifestyles and travel, but also the desire to access aged-care at home.

According to the latest IbisWorld industry report, Franchising in Australia, "Industry growth areas include service-based franchises such as health, nutrition and well-being, along with aged care services and recreational services.

"These types of franchises require at least 20 to 30 establishments to generate enough revenue to cover marketing and over-head costs."

It's good news for franchisees that service time-constrained customers with high disposable incomes.

Retail outlook

Strong competition in well-established industries such as the food sector will continue. It is expected that emerging niche areas like the health and wellbeing services will be less affected by competing brands.

IbisWorld suggests profitability growth can be achieved through greater market penetration, expansion or diversification of the goods or services on offer, and of course by making general cost reductions.

As the Franchising Australia 2014 report from Asia Pacific Centre for Franchising Excellence outlined, online retailing is still being used by fewer than 50 percent of franchise systems (45 percent). But that should rise to about 65 percent as more franchisors implement their plans to trade online.



Figure 3

According to a recent survey from the Commonwealth Bank, retailers in general are forecasting online sales growth of 20 percent. The CommBank Retail Insights report indicates the value of the average online sale has risen 14 percent, year on year.

Online retailing will allow franchisees themselves to reach customers in new regions, particularly in rural areas, but handling the allocation of business, particularly when there are local bricks-and-mortar stores, remains a challenge for franchisors.

Key sectors

The key sectors remain retail trade and accommodation and food services.

Despite economic uncertainty and fluctuating consumer sentiment, the size of the retail arena - which accounts for 27.1 percent of the sector - has grown since 2010. But there's less profit to be achieved because of the higher wages and penalty rates introduced.

When it comes to the staffing of franchised outlets and businesses, while individual franchises will require their complement of full-time, part-time and casual staff, the sector is expected to follow the national trend for increased part-time and casual positions.

Fast food chains have helped drive the growth of the accommodation and food sector (18.1 percent). Healthy eating in particular has boosted this part of the franchising arena, which includes coffee shops and hotels.

At 14.7 percent of the franchising sector, the administrative and support services includes domestic and commercial cleaning, gardening services, office support and travel agencies.

Personal services (10.5 percent) have grown because they are predominantly low-cost, mobile operations that find it easy to attract new franchisees. The dominant services here are home-based - technology and outsourcing trends have boosted their growth. Australia's pet services market has been fuelled by demand for pet-care merchandise.

The remaining 29.6 percent of franchised businesses is made up from services such as real estate, transport, rentals, financial, education and training.

The rule of law

The sector is governed by the Franchising Code of Conduct which is regulated by the Australian Competition and Consumer Commission. In January 2015 a new revised Code came into force, and this updated regulation is expected to strengthen relationships between franchisees and franchisors. There's a great focus on both parties acting in good faith, and for franchisors a requirement for greater transparency and disclosure.

Franchising Growth Sectors:

Here are some of the growth sectors that will open up opportunities for business ownership; some you may have considered, others might surprise you.

Cafes and Coffee:

IBISWorld's Cafes and Coffee Shops in Australia (March 2014) industry report describes the coffee culture as robust, and responsible for driving the café business through the tougher economic times of recent years.

And according to Euromonitor International's report, Cafes/Bars in Australia (November 2013), Australia's love affair has contributed to "the four percent foodservice value growth experienced by cafes and two percent value growth of specialist coffee shops".

The report states growth within chained cafes is forecast to outpace that of independent cafes during the 2012-17 period. That's good news for the multitude of franchises operating in this sector.

Healthy Eating and Asian Cuisine:

As the IbisWorld report *Fast Food Services in Australia, June 2014* reveals healthy eating has driven change in this sector: a decline in the share of revenue among traditional fast food operators has been matched by increased revenue in the healthier fast food categories.

It's been an underdeveloped sector, but now the vast range of dishes available across the Chinese, Indian, Japanese, Thai and Vietnamese cultures are contributing 10 percent of revenue to the fast food sector, reports IbisWorld.

This sub-division of the sector is also benefiting from the focus on healthier eating.

KIOSKS, Teas and Juice:

The value of foodservice sales in street stalls and kiosks operating in chains is expected to grow from 396.2 million in 2012 to 482.7 million in 2017.

A Euromonitor report indicates that over this period these operators are likely to record a stronger performance than will independent businesses.

These kiosks offer a limited menu, and leverage the customer's impulsive snack purchasing behaviour.

Aged Care and Retirement:

The global population is ageing, and Australian demographics are following suit. A number of franchised businesses are providing different levels of aged and nursing care for home-based clients, providing them with a lifestyle that allows them independence while providing support for their particular needs.

It's worth noting too, our senior citizens have money to spend. Australian retirees are the wealthiest in the world, with the average wealth almost doubling in one generation, due particularly to increased home ownership.

And this makes retirement living and leisure another attractive proposition.

Wellbeing and Fitness:

The preventative health and wellness sector is set to see the greatest growth over the next 20 years, according to Deloitte. This could be a business geared to helping people lead more active lives through to diagnostic centres and allied health professionals.

And more than four million Australians are participating in some form of fitness activity, typically between the ages of 25 and 34, and with women overtaking men in the participation stakes.

The gym sector is well represented by big brands: Fitness Australia's membership data from 2011 shows 45 percent of businesses were either company owned or franchised.

Mobile Businesses:

Busy Australians are looking for time-saving services. So community and personal care - the domestic services, dog walkers, personal shopping services - are set to grow by 4.79 percent overall, predicts Deloitte. The convenience factor is increasingly important and this broad sector covers services as diverse as lawn mowing and dog washing, handyman repairs, couriers, coffee vans and food trucks and safety services.

Finance:

Deloitte predicts a growth rate across finance business models of 5.11 percent. There will be plenty of opportunities for new products, wealth structuring and estate planning, the company suggests, based on estimates by the Australian Bureau of Statistics that Australia's 9.3 million homes are now worth \$5 trillion.

This fits neatly into the trend of the ageing population too, with mature citizens looking to manage their money wisely.

Could one of these sectors be right for your investment? Each has pros and cons, suits differing skills and personalities, and offers franchisees a variety of ways of working. Which suits you? How will you choose to spend your day?

Franchising is a robust, vibrant and exciting part of the economy, accounting for approximately 4% of all small businesses in Australia, with total annual sales revenues of \$146 billion and an optimistic outlook.

Despite a relatively flat economy and retail environment, Australia's franchise sector continues to grow in total sales turnover and employment and its franchisors are confident of further growth in the next 12 months.

According to the biennial survey of franchising in Australia, total annual sales revenue for the country's entire franchise sector is estimated at \$146 billion, up from \$144 billion in a previous survey in 2014.

The total number of people directly employed in business-format franchising in Australia also continues to rise now reaching 472,000 permanent, part-time and casual employees, up from 461,000 two years ago.

The Franchising Australia 2016 survey, undertaken by Griffith University's Asia-Pacific Centre for Franchising Excellence and supported by the Franchise Council of Australia, marks the 10th installment of this definitive benchmarking study of Australian franchising. The survey dates back to 1998 and has been updated every two years since.

The headline findings of the Franchising Australia 2016 survey are being released at this week's Franchise Council of Australia National Franchise Convention in Canberra. The full report will be available in January 2017.

Mr Bruce Billson, Executive Chairman of the Franchise Council of Australia, said franchising is a robust, vibrant and exciting part of the economy, accounting for approximately 4% of all small businesses in Australia. He said the survey results show Australia's franchising sector has continued to perform strongly, against the backdrop of relatively slow economic growth.

"The Franchising Australia 2016 survey points to a maturing sector, holding its own in a transitioning economy following the end of the mining boom," he said. "Total sales turnover for the sector has risen slightly, while employment has steadily risen and created more permanent full-time jobs. Franchisors are also predicting growth in franchise numbers over the next 12 months," Billson added.

Despite the difficult economic environment, franchisors have once again met or exceeded growth targets set in 2010, indicating franchisors were realistic in their goals and executed their growth plans effectively. Overall, and especially compared with the private business sector as a whole, the franchise sector has performed strongly – providing further evidence of the robustness of the franchise business model. Over the last 12 months, on average, franchisor revenue has increased by 17 per cent and franchisor profit has increased by 22 per cent – outperforming last year's forecasts of 13 and 18 per cent respectively. Franchisee revenue increased by 12 per cent (exceeding last year's forecast of 10 per cent) and profit increased by 13 per cent (meeting last year's forecast). As a comparison, the ninth edition of the PwC Private Business Barometer showed that private businesses estimated their sales grew by an average of six per cent and profit by seven per cent over the previous 12 months.

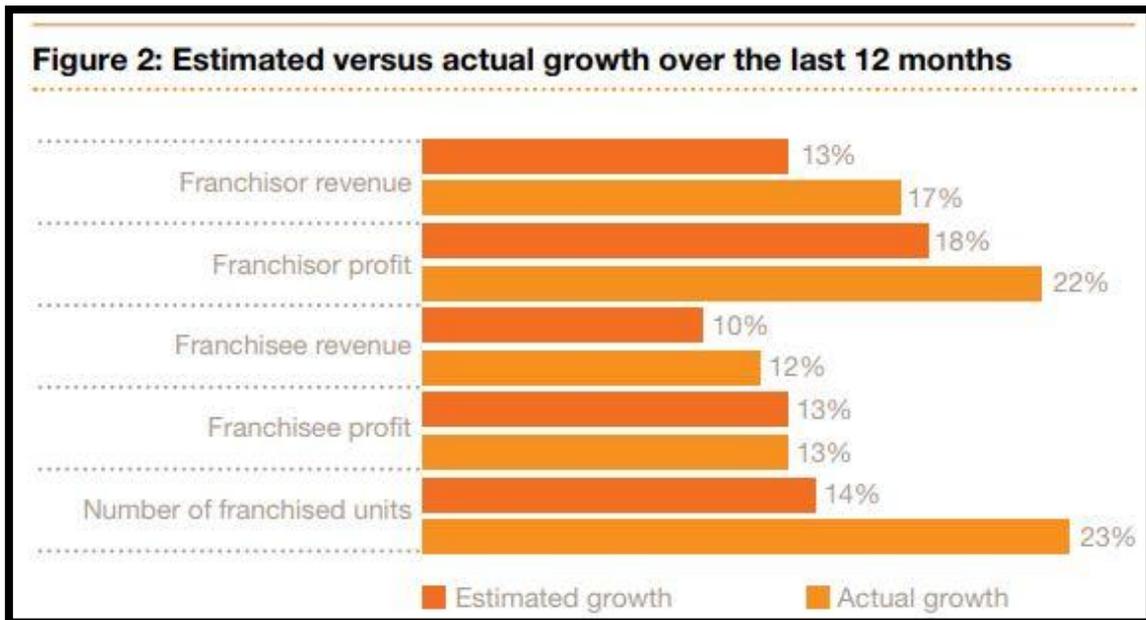


Figure 4

Growth through innovation There have been some fantastic stories of successful innovation driving growth within the franchise sector. In the fitness sector, which some may have previously said was saturated, Anytime Fitness has been a leader in promoting a different business model – twenty-four hour fitness.

Table 3: Mean growth over past 12 months

	Total number of units (franchise & corporate)		Sector	
	20-99	100+	Retail	Non-retail
Franchisor revenue	23%	9%	22%	12%
Franchisor profit	27%	15%	26%	18%
Average franchisee revenue	13%	11%	11%	13%
Average franchisee profit	13%	11%	13%	12%
Number of franchised units	35%	9%	36%	9%

Figure 5

The exponential growth of this business (discussed in more detail on pages 21 and 22) has proven that even operating models that have existed for a long time

can be challenged and the results successful. Another example of innovation in the sector is with the pizza brands, who have challenged the junk food stereotype by making efforts to achieve the Heart Foundation tick, Halal Accreditation and introduced executive chefs to develop their recipes. We are also seeing franchisors utilising smart phone check-in capabilities to drive traffic to their stores. 7-Eleven and KFC are using digital coupons to attract customers to their retail stores by offering special deals. Although not a franchise, the Commonwealth Bank are offering vouchers to people who check-in when opening a new bank account at a branch – proving that even non-retailers can take advantage of these mobile capabilities.

Conclusion:

Franchisors have indicated that they would like to see increased government support in financing new franchisees, funding for franchisee training and finalisation of the questions surrounding State versus Federal franchise legislation. In relation to funding, The United States has several initiatives for funding incoming franchisees including acting as guarantor to bank loans where incoming small business owners are having difficulty gaining financing. It seems that franchisors in Australia want a similar programme. There is also a huge opportunity for an Australian bank to increase its franchise sector lending through more flexible lending practices, acknowledging the strength of the franchise model. It does not make sense that the sector continues to outperform the rest of the business community, and has many risk-alleviating attributes and yet banks make it more and more difficult for franchisees to get funding.

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