



2022 FLDC

FRANCHISE LEADERSHIP & DEVELOPMENT CONFERENCE

A Lot of Change Is Happening and It's Complicated

 **FRANdata**

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INTERNATIONAL FRANCHISE ASSOCIATION



FRANCHISING IN 2023

Macroeconomic Outlook

What will shape consumer spending for 2023 and beyond

Capital Access

How lender credit boxes are changing

Impact on Franchising

What it means for prospects, support, and your 2023 planning

World Economy: Overview

Inflation driving downturn around world

UNITED STATES

Inflation
Slowing economy,
labor issues,

EUROPE

“Deep recession”
Energy conflict with
Russia
Devaluing currency
Out of control inflation
– 9.9%
Public sector job cuts
Ukraine War

RUSSIA

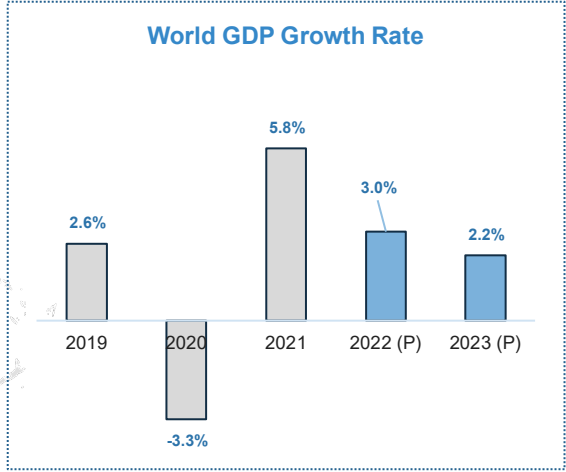
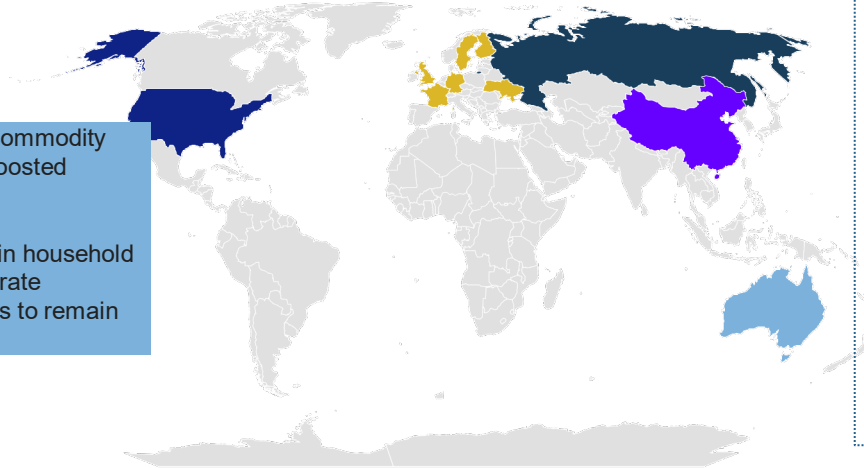
Trade war and
sanctions
Ongoing war with
Ukraine
Rising cost of
imports

CHINA

COVID-19
Slow GDP growth
Collapse of housing
market
Trade sanctions
Taiwan tension

AUSTRALIA

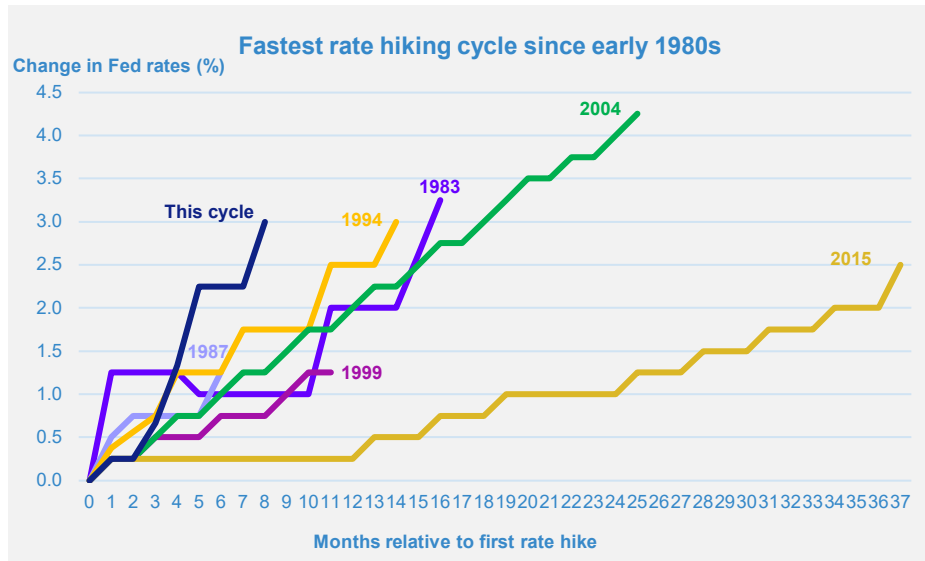
Higher commodity
prices boosted
exports.
Inflation
Decline in household
savings rate
Oil prices to remain
high



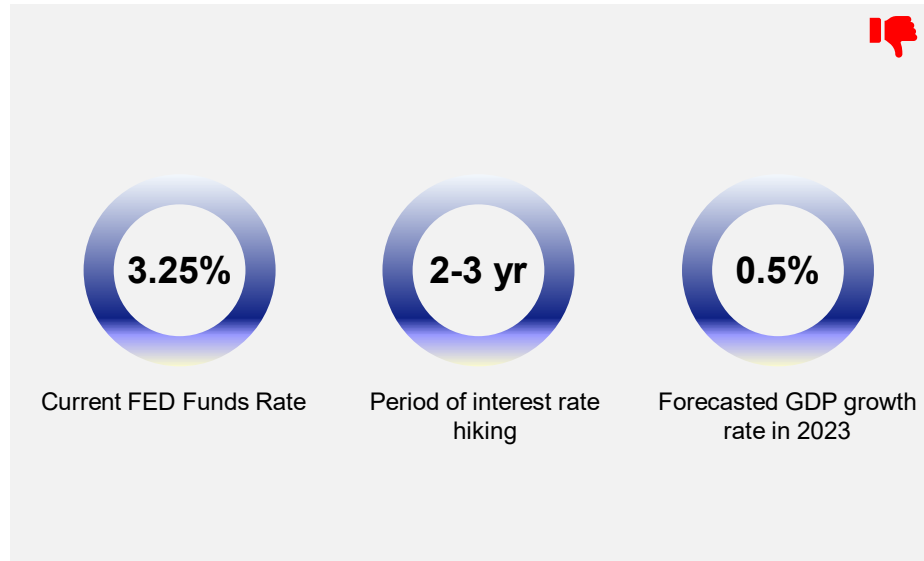
Source: FRANdata Research, OECD Interim Economic Outlook September 2022

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FED not backing down from fighting inflation



Source: FRANdata Research, [Charles Schwab](#)



Rising rates dampen domestic spending

Cost of fighting inflation: GDP growth and negative sentiment

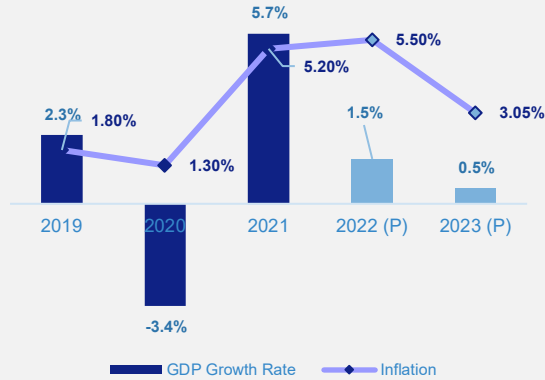
↓ Projected GDP growth rate 0.5%

↓ Inflation will slightly improve in '23 but still high

↓ High interest rate to keep inflation in check

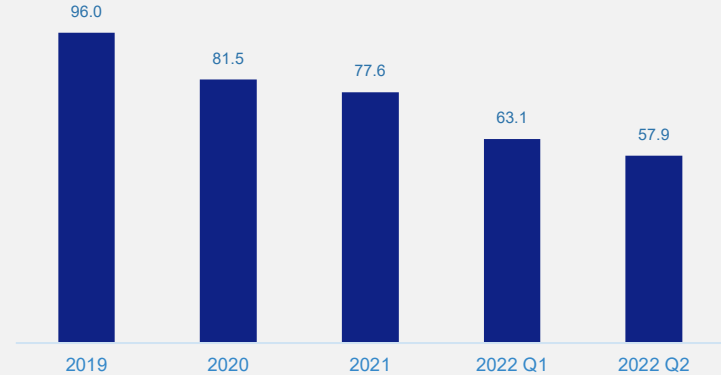
↑ Financial institutions are healthy

US GDP Growth Rate & Inflation



Source: FRANData Research, OECD Interim Economic Outlook September 2022

Consumer Sentiment Index

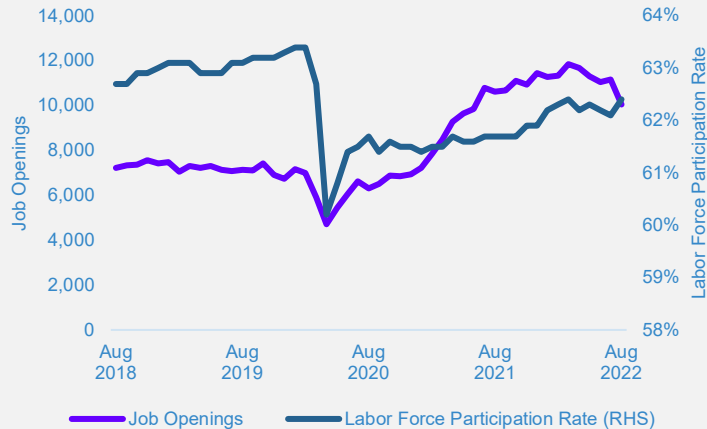


Source: [University of Michigan](#)

Labor Market

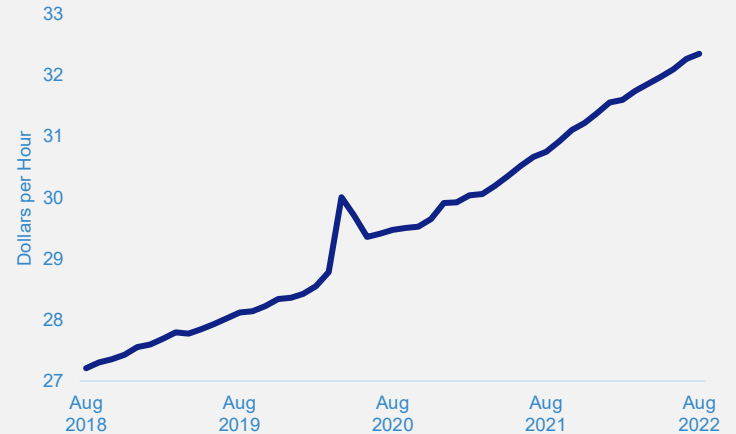
Labor supply and cost of labor will continue to be a challenge

Job Openings & Labor Force Participation Rate



Source: Bureau of Labor

Average Hourly Earnings



Source: Bureau of Labor

Workforce shortage and wage inflation are top challenges for small businesses in 2022/2023 – 88% franchisees are unable to find employees; Wages increased by 4% in 2022

Household Income

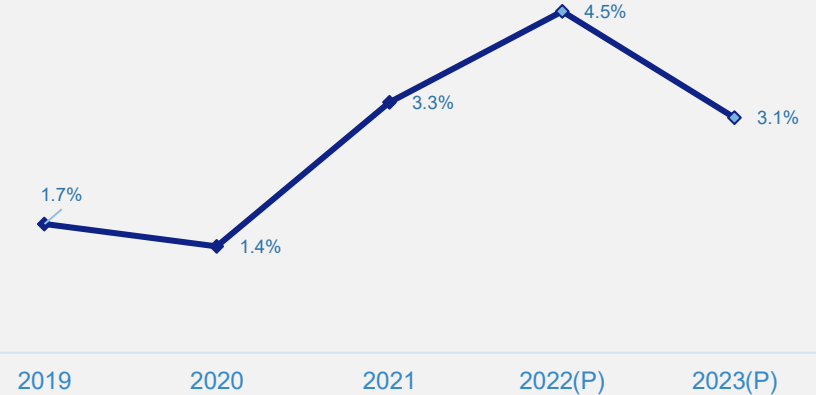
Declining ability and willingness to grow spending

Real Disposable Income and Savings Rate



Source: U.S Bureau of Economic Analysis, April 2022

Core Personal Consumption Expenditure*



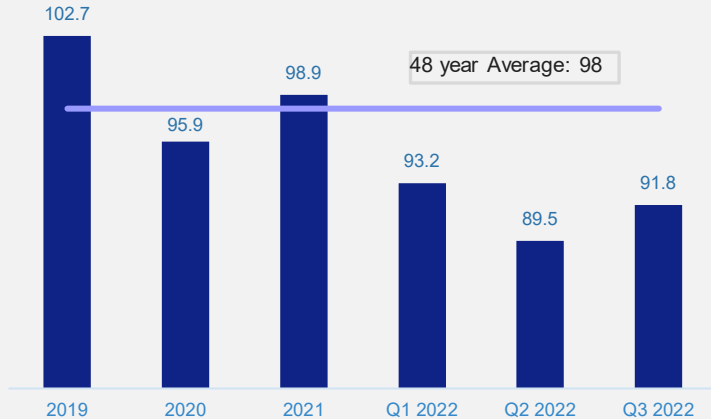
Source: U.S Bureau of Economic Analysis, April 2022

We're looking at negative discretionary cash flow for the first time since the 2008-09 financial crisis

Small Business Impact

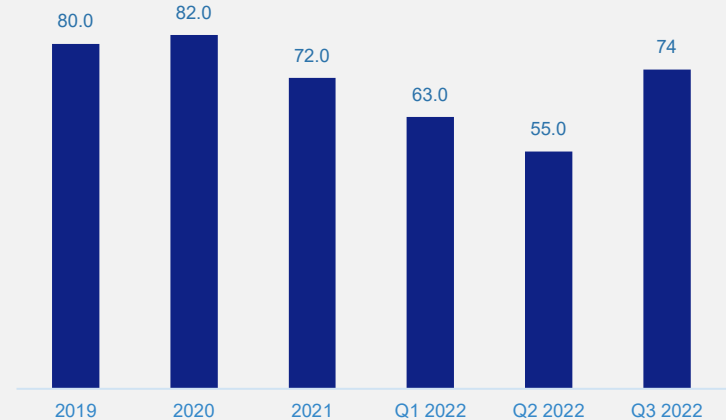
Small businesses are more uncertain and risk averse

Small Business Optimism Index



Source: NFIB, FRANdata Research

Small Business Uncertainty Index



Source: NFIB, FRANdata Research

As optimism for small businesses declines and uncertainty about future increases, small businesses will reassess their growth and expansion plans for 2023

No rockets on horizon to propel recovery

More likely a “*pasta bowl*” recovery

What we know

- Slowing economic growth
- Rising interest rates
- No fiscal stimulus likely
- Labor wage rates sticky

What matters

- FED’s singular focus on inflation
- When will unemployment rise
- When household income stabilizes



What we don’t know

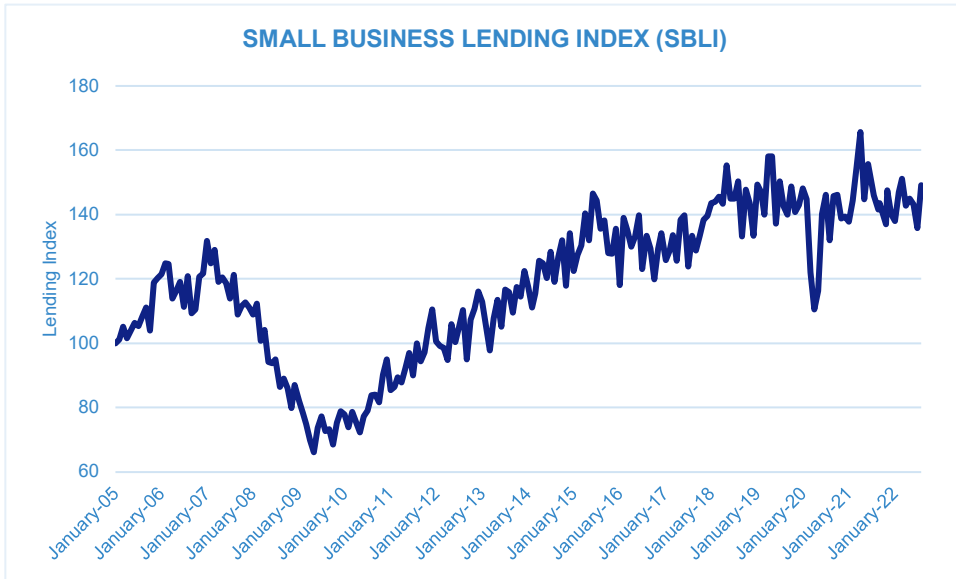
- How long and how deep a downturn
- When supply chain and product shortages rebalance

What we think

- Consumers will be very price conscious
- Business unit margin erosion will continue beyond 2023
- Best practices will change more frequently driven by data analysis

Small Business Lending Index

Banks more selective and offer tougher terms



Source: Equifax, FRANData Research

Availability of capital



Accessibility of capital

What lenders want to know

Lenders more risk averse



How is the brand dealing with inflationary pressure?



What is the impact of increased cost of capital on bottom line?



Is brand prepared to survive economic downturn?



How is the brand helping franchisees deal with macroeconomic challenges?



How will the demand of brand's services/goods change in 2023+?



Does the business model hold up to a pro forma stress test?

How lenders are adjusting

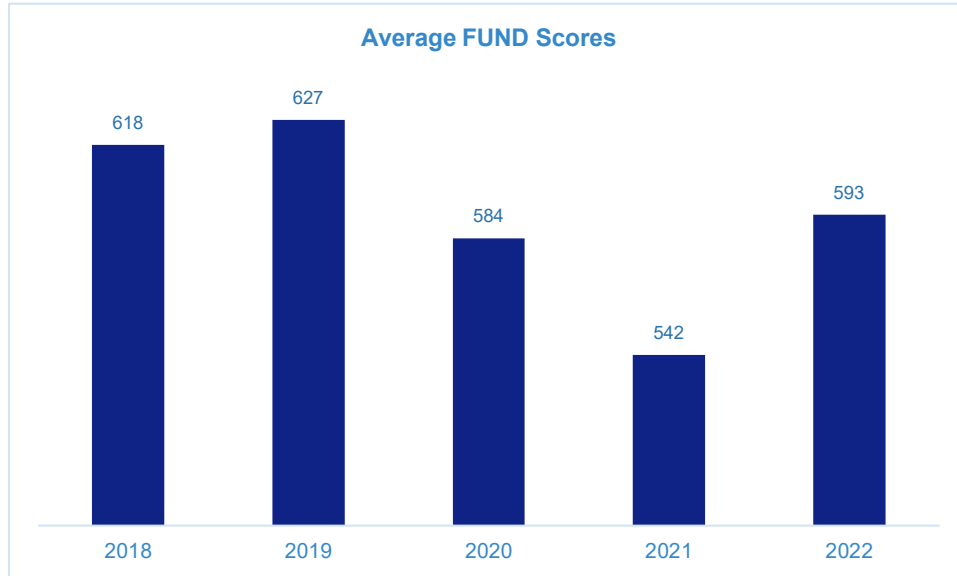
Lenders will have lower risk tolerance

	Pre 2020	2020-2021	2022-2023
Past Performance History	Very Important	Very Important	Somewhat Important
Cash on Balance Sheet	Very Important	Very Important	Somewhat Important
Loan repayment history	Very Important	Very Important	Somewhat Important
Viability of business model	Somewhat Important	Somewhat Important	Very Important
Revenues & Margin	Somewhat Important	Somewhat Important	Very Important
Impact on cost when delay in opening new units	Somewhat Important	Somewhat Important	Very Important
Change in Buildout and Opening Cost	Somewhat Important	Somewhat Important	Very Important
Consolidation through M&A	Somewhat Important	Somewhat Important	Very Important

Very Important
Somewhat Important
Not Important

FUND SCORES

Most franchise systems are prepared to handle economic downturn



Source: FRANdata Research

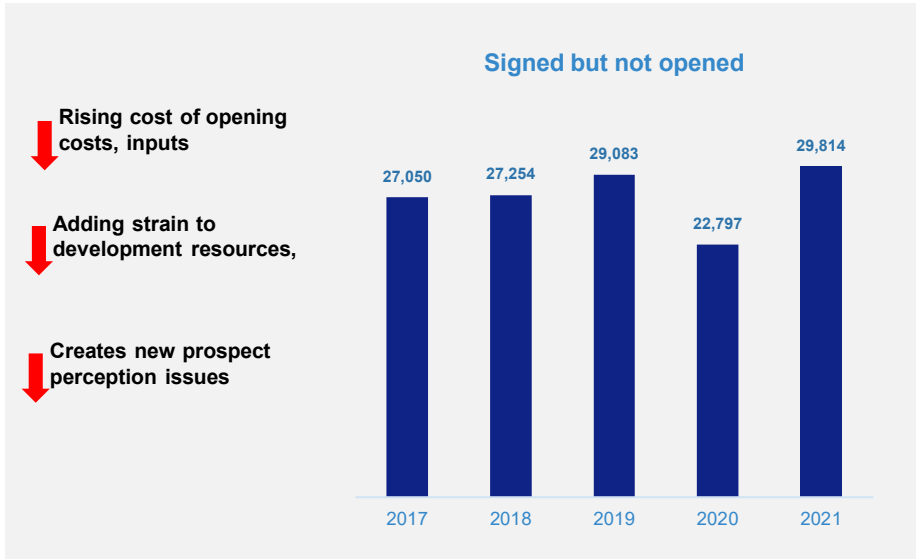


***Transparency and
performance driving
access to credit***

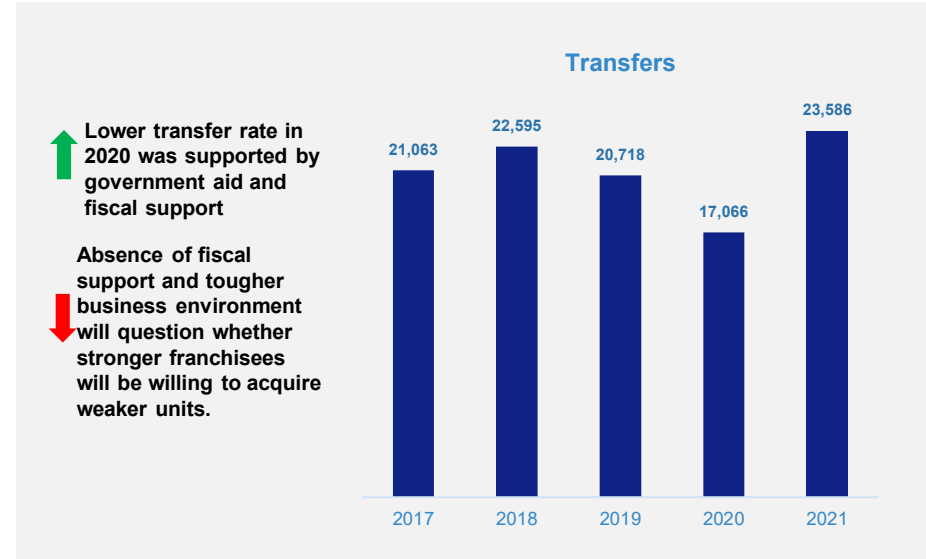
Post pandemic FUND scores indicate brands likely to have challenges getting funding in 2023

How franchising is being impacted

More closures, transfers, opening delays



Source: FRANdata Research



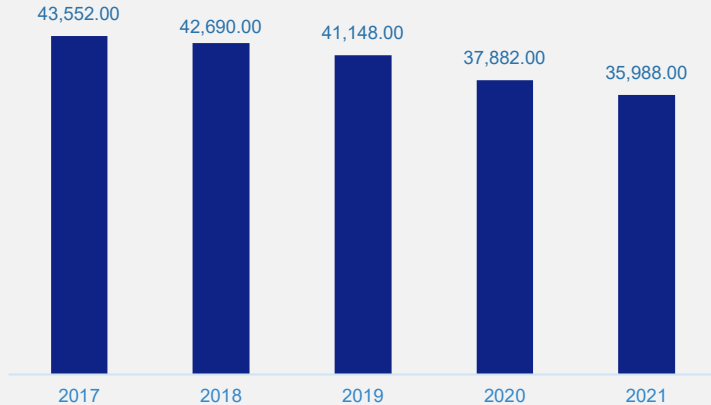
Source: FRANdata Research

Government aid buoyed franchising but has ended
Rising costs hurt initial investment, unit economics

Switching Jobs/Careers

History shows a less movement in early stage of downturn

New units opened each year



Source: FRANdata Research



New unit development is below pre pandemic period



Negative sentiment and high uncertainty will impact new development



Cost of development has increased due to inflation & high interest rate

Economic concerns, inflation driving initial investment up, and increased cost of capital will make prospects hesitant

Key Takeaways

*How should you plan
for year 2023?*



Franchise Outlook 2023

2021 was pandemic driven; 2022 has been inflation driven; 2023 will be recession driven

Offering models and changing operations

- Consumer preference shifts and input cost pressures changing offering models and support structures



Consumers more price sensitive

- Price increases to protect margins getting more difficult



New pool of franchisees

- Layoffs will lead to more prospects but when?



Tougher lending standards

- Eroding margins, higher cost of capital



Legal impediments

- New regulations such as AB 257 will continue to challenge brands in unique way



Stretched working capital

- Remodels and new capx requirements get delayed as working capital declines



How brands will deal with these challenges

Focus shifting to preserving margins and making changes, not just on driving growth

New Model, Remodel, Technology Innovation

Weighing the cost but also the necessity



Consolidation

Avoiding failed units means MUs buying units, zor buybacks.



International Expansion

With US relatively stronger, international expansion less appealing



How Franchising will look in 2023

Marketing

Changed consumer behavior more price sensitivity implies



Unit Economics

Stressed consumers and rising input costs make margins a primary focus



Lender Needs

Higher prospect standards and better system transparency are musts



What does it mean for franchising?

Length of downturn in your sector will determine your actions

1

Innovation, fundamental changes will happen faster

2

Multiple economic challenges converging; decisions will require better information

3

Lender underwriting changes demand more transparency and better performance



Thanks

Did this change the way you
think about franchising in
2023?

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