Franchise Times®

www.franchisetimes.com The News and Information Source for Franchising November/December 2008

It will take some time for the credit freeze to cycle through. In the meantime, here are some tips to help you out. Perhaps the best one: Don't panic.

Credit contraction

Financing opportunities in tough times

I don't have to tell you franchise financing is tight. All you have to do is open up The Wall Street Journal, local newspapers or trade magazines to understand the present credit crunch. In my 30 years of working in the franchise space, I have seen many contractions and have been through many periods when franchise financing was virtually nonexistent. What is unique about this situation is that the credit crunch is not just affecting franchise financing, but financing in general. It will take time to cycle through this contraction. Yet there is no reason to panic, because there are still ways to get financing done.

The following are some of my observations on the current financing conditions and suggestions on how to respond to and outlast the current market downturn:

Package your business

The way you package your franchise business (whether it be a capital intensive franchise or something that is more service oriented) will affect the process of getting financing. When you are meeting with potential lenders, do not position yourself as a franchise or restaurant business or a narrow segment. Position yourself as a small business—a business that has a huge growth potential and is backed by superior management. I do not ask potential lenders who are not in the franchise or restaurant space, "Do you do restaurant lending?" Instead I prefer to ask, "Will you do multi-unit retail lending?" or "Will you look at small business or middle market lending?"

Look at potential lending sources

We know the major capital lenders that are still in business are fairly tight in their lending, but they are still providing some financing opportunities. Even though they look at credit with a higher degree of scrutiny, the lenders are continuing to make loans.

There are also other lending sources to consider. The most viable opportunities are with the small- and middle-market banks. For the most part, these groups are not part of the capital market crunch and are the backbone of American lending. These groups include local community banks, regional banks and large metropolitan concentrated banks. They still have strong deposits and need to make loans to keep their banks profitable. Obviously, scrutiny will be tough, but the most important thing to look at is what type of loans these banks will make.

Get to know your bank. If the bank focuses on real estate related loans, then package your business as a real estate type loan (such as a significant leasehold interest). If the bank focuses on owner operated loans, then package your business as owner operated.

Franchisors' help

As stated many times in this column, franchisors need to provide some type of credit enhancement if they expect large franchise finance companies to lend into their system. In most cases, it will not be possible to get remodel and equipment monies from these type of sources without some type of franchisor enhancement. These enhancements can take many forms: limited guaranties, remarketing agreements, pledged collateral, rate buy downs—the list and options are very long.

Real estate prices

Real estate prices have softened and vacancy rates have risen. Landlords with suitable financing and decent liquidity are providing deals

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to prospective tenants with terms I have not seen before. These terms include significant landlord leasehold allowances; short-term leases with reasonable outs; and assistance with fixture, furniture and equipment financing. In general, landlords are offering favorable positions to get dead spaces occupied. The landlord may be one of the best sources for the franchise community in this current market. Try to get into spaces with little money down and by all means, limit your risk.

Self-directed retirement accounts (401(k)s, IRAs, etc.)

With some careful planning and the use of experts, retirement accounts may become available for investment in small, closely-held companies. Look at these accounts as sources of available funding. With the stock market evolving in triple-digit declines on a daily basis and the overall market volatility, franchise small business investments may become more and more attractive to the average investor. There are specific companies that specialize in this technique.

Private placement

Private placements may be a great source of equity for the expanding franchise company. Once again, people have limited avenues for investing in growth and high yield investments. Individuals may be more than willing to look at a well developed and structured private placement for investment in franchise concepts and franchise unit development. A well structured private placement memorandum can be compelling. One important thing to keep in mind is most private placements require the owner to do the investor selling.

Non-traditional approaches

During a market downturn and financing contraction, it is worth considering non-traditional approaches. Some non-traditional approaches include:

- Joint ventures with other concepts;
- Someone may want to develop your concept in conjunction with some other business they may have;
- Managing other people's franchises, if you have a good infrastructure in your own existing company;
- Ways to team up with public companies that may need to have some type of growth vehicle; and
- Foreign investors.

Shifting of risk

When there is a tight credit market, one goal should be to try to shift the risk. Risk is really what creates problems in difficult economic times. Anything you can do to shift the risk (i.e., put less money into a project, have someone else finance it; or have a smaller piece with less risk) is certainly something to evaluate. You may give up something on the upside, but in today's market you are probably more concerned about protecting on the downside rather than gaining on the upside.

Leveraging market share

Franchise concepts that are going to succeed in today's economy are going to have to steal market share vs. attracting new customers. When you look at your financing, locations and business proposition, always think of market share vs. attracting new customers to your market segment. Today's retail market is contracting, not expanding. You don't have time to educate new consumers. The cost of attracting new customers to the market segment is much greater than converting shares from someone who is already a consumer in your market segment.

Remember, there are opportunities in today's market place. It is a matter of re-educating yourself and positioning your business. Granted, there are no easy solutions, but solutions do exist. FT

Randy Evans, a partner at Krass Monroe, contributed to this month's column.

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