

# Your business: cream on top costs a little extra

Proven franchises supported by promotional campaigns cost a lot more than basic entry-level enterprises, writes **Alexandra Cain**.

You get what you pay for - that's the message from experts to anyone considering buying a franchise.

At one end of the scale is a McDonald's franchise, widely considered a licence to print money, which is reputed to cost about \$1 million. At the other end is a basic lawn mowing business, which might set a franchisee back less than \$20,000.

Of course, there are thousands of different options in between, but the main difference in price reflects the strength of the brand, the training offered and the potential income that can be earned through the franchise.

Franchise expert **Greg Chapman**, director of business consultancy **Empower Business Solutions**, says "if you buy a Jim's Mowing franchise, you're not getting a lot".

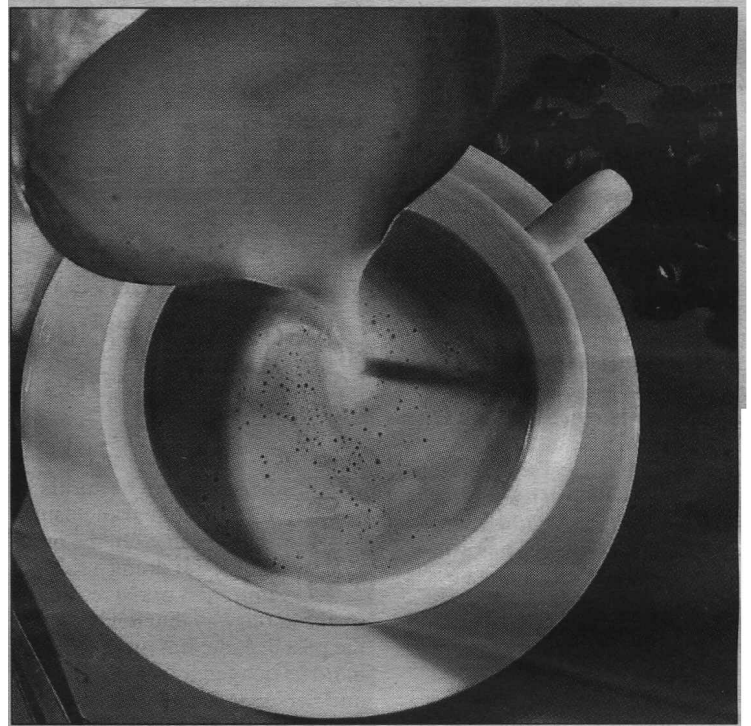
"For around \$15,000 you'd get a territory, a small amount of training and some equipment, and you will be encouraged to do your own marketing to top up the enquiries that come directly from Jim's."

"You'd pay a bit more, say \$20,000, for an established franchise, with maybe 100 homes on the books, but you'd have to do less marketing and you'd have an immediate income," he says.

"Jim's is a mobile service, so there are few costs around fixtures and fittings - the franchisee is mainly paying for the van and the trailer," says KPMG's partner specialising in franchising, Carlo Pasqualini.

"The fee also includes a small amount of training, which is focused on service and how to approach the customer," he says.

In contrast, says Chapman, a McDonald's franchise, what he calls "the big daddy" of franchises, will cost between \$500,000 and \$1.5 million, depending on the location and the revenue generating potential of the store.



## A cut above

- ❑ Ongoing royalty fees cover the right to use a brand and research and development.
- ❑ The higher the potential revenue from a franchise, the higher the royalty fees payable.
- ❑ The fees for buying into a franchise are unlikely to fall, except as an incentive to invest in new systems.

This fee will generally cover the cost of the land and building of the store, as well as fit-out. It also covers the cost of access to the powerful McDonald's brand, as well as ongoing marketing, including television advertising.

"When you include things like the cost of tables, ovens, fryers, fridges, and the fact that these things break, you can see operating a McDonald's is much more capital intensive than a mowing business," says Pasqualini.

The initial fee for a McDonald's also covers its proven systems and procedures, which detail everything from shutting up to sweeping the floors.

"But the higher the cost of the franchise, the more opportunity to make money," says Pasqualini. "And paying for proven systems and procedures means you're much more likely to be a success," he adds.

Aside from the initial fee, franchises generally expect their franchisees to pay an ongoing royalty fee, which covers the right to continue to use the brand, as well as things like research and development. This fee is usually between 10 per cent and 15 per cent of ongoing revenue. Again, the higher the royalty payable, the higher the potential revenue the franchise can generate.

"Ongoing royalties may be impacted by the marketing campaign. If television is involved, the royalty is likely to be much higher, especially if the campaign is national. If the marketing campaign is more about local radio and newspaper advertising, then the royalty will normally be lower," says Pasqualini.

Ian Martin is group chief executive of Gloria Jean's Coffees, a highly successful coffee shop franchise. Martin says his franchisees pay an initial \$59,000 fee, which covers the cost of using the trademark. There is also a \$12,000 initial training fee, and an ongoing 8 per cent royalty fee, which is low compared with many other franchise models. This includes a 2 per cent fee covering advertising and ongoing marketing and a 6 per cent ongoing fee for the use of the system, which covers improved in-store operating procedures and new product development.

Gloria Jean's Coffees releases two new promotional drinks each quarter.

But, says Martin "franchisees can't just write us a cheque. There is a rigorous five-step interview and training process potential franchisees have to pass before they can become a member of the Gloria Jean's Coffees family".

Every new franchise partner from around the world must also attend Gloria Jean's Coffee University in Sydney - and new franchise owners are expected to fund themselves to get there and participate in the four-week program.

The experts that *The Australian Financial Review* spoke to agree that in general, the cost of buying into a franchise has remained the same in recent years. Says Chapman: "I don't think fees are increasing significantly."

He says, good franchisees are becoming hard to find as a result of the strong economy and full employment, and this could drive the cost of the average franchise down. But this trend is counteracted by increasing rental prices and inflation.

"The cost of franchises is unlikely to come down," says Pasqualini. "But if the franchise has just started, and they need to attract lots of franchisees to create a critical mass, you might find costs are reduced as an incentive to buy in."