

Franchisors Cautious of Economic Environment

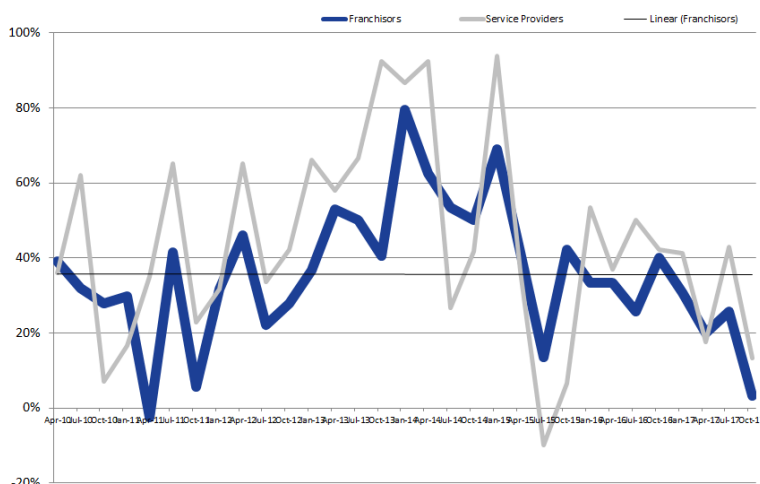
Franchise Consultants' October 2017 *Franchising Confidence Index* demonstrates a strong shift in confidence levels, with changes prevalent in sentiment toward general business conditions, and franchisor growth prospects. Conversely, sentiment toward the availability of suitable staff (which has been viewed as a key ongoing challenge) and locations saw a positive upwards shift.

Both Franchisors and Service Providers similarly declined in sentiment toward **general business conditions**. Franchisors (net 3%) decreased from the previous quarter (26%). Service Providers decreased more markedly from a net 43% in July to 13%.

The Franchisor net 3% positivity in outlook for general business conditions was in line with that of other research involving general business. The ANZ Business Outlook decreased to a net 0% in September (down from 43% in June). Meanwhile, the NZIER business survey decreased significantly from 18% in July to a net 7% in October.

Our experience, now involving some 31 consecutive quarters (over eight calendar years), indicates franchisors are normally more positive toward future general business conditions compared to datasets involving other organisational forms.

GENERAL BUSINESS CONDITIONS



RESULTS SUMMARY TABLE

	Franchisors										Service Providers									
	Jul-15	Oct-15	Jan-16	Apr-16	Jul-16	Oct-16	Jan-17	Apr-17	Jul-17	Oct-17	Jul-15	Oct-15	Jan-16	Apr-16	Jul-16	Oct-16	Jan-17	Apr-17	Jul-17	Oct-17
General business conditions	14%	42%	33%	33%	26%	40%	31%	20%	26%	3%	-10%	7%	53%	37%	50%	42%	41%	18%	43%	13%
Access to financing	19%	21%	30%	21%	0%	15%	-8%	-18%	-8%	-13%	30%	27%	53%	37%	-5%	0%	18%	0%	-21%	-7%
Access to suitable franchisees	-8%	-16%	0%	-6%	11%	12%	10%	-10%	13%	-20%	40%	33%	20%	21%	5%	21%	41%	24%	36%	7%
Availability of suitable staff	-6%	0%	-7%	-9%	-12%	-13%	-3%	-26%	-32%	-14%	30%	0%	0%	11%	5%	-5%	-6%	0%	-7%	7%
Availability of suitable locations	-3%	-6%	-16%	3%	6%	-13%	16%	17%	-5%	11%	20%	20%	0%	53%	5%	26%	12%	6%	21%	20%
Sales levels per franchisee	32%	53%	52%	39%	51%	63%	56%	49%	51%	43%	10%	7%	53%	-21%	30%	42%	53%	41%	43%	13%
Operating costs per franchisee	-16%	-6%	-19%	3%	-6%	0%	-13%	0%	-15%	-21%	-20%	-7%	20%	26%	5%	-11%	0%	-29%	-21%	-27%
Franchisee profitability levels	19%	26%	44%	21%	40%	49%	44%	40%	18%	7%	20%	27%	33%	47%	40%	21%	35%	0%	29%	-7%
Franchisor growth prospects	35%	47%	56%	45%	46%	57%	59%	48%	45%	28%	0%	20%	47%	47%	50%	53%	47%	41%	43%	7%

*The figures indicate 'net' confidence. Net' confidence is the difference between those reporting 'better' and 'worse'

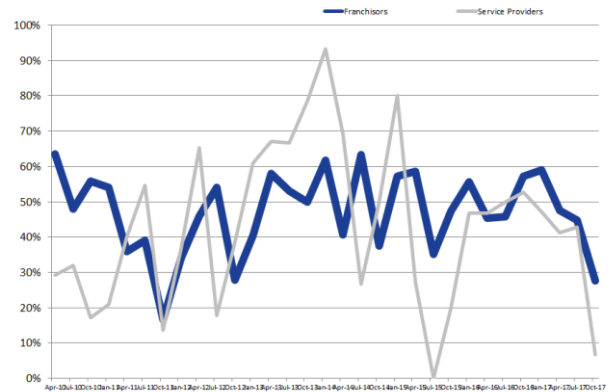
Franchisor sentiment for **franchisor growth prospects** dipped substantially from what had been a stable sentiment over the past four years, to net 28%. Service Providers were similarly sombre at a net 7%, its lowest level since July 2015.

Franchisor sentiment toward **access to suitable franchisees** has always been challenging. After seeing increased positivity in July, October has shown a marked decrease in confidence down from a positive net 13% to net negative 20%. Service Providers were of similar sentiment dropping to a net 7% from net 36%.

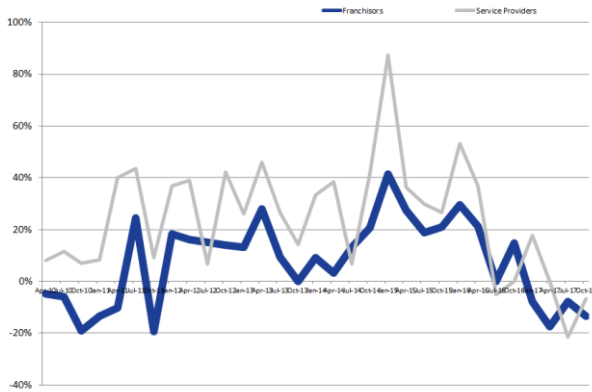
Franchisor and Service Provider sentiment toward **access to financing** remains a challenge, with franchisors slightly less positive at a net negative 13%, down from a negative 8%. Service providers sentiment was elevated from a net negative 21% to a negative 7%.

Franchisors sentiment this quarter towards **accessing suitable locations** bounced back from a dip in July to a positive net 11%, up from a net negative 5%. Service Providers outlook remained stable at a net 20% down from net 21%.

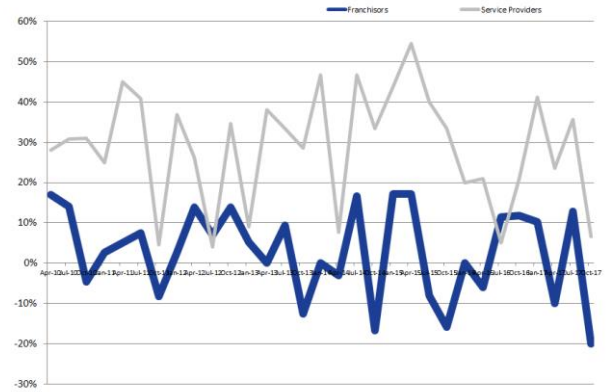
FRANCHISOR GROWTH PROSPECTS



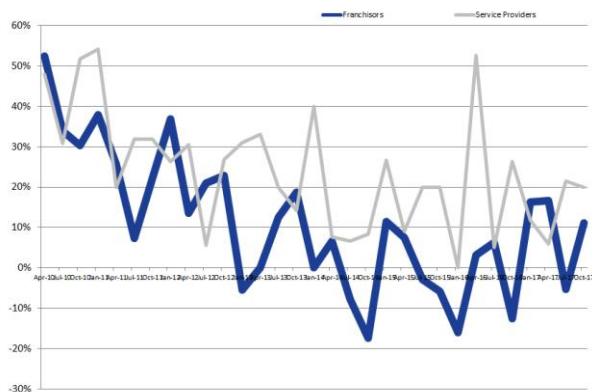
ACCESSTO FINANCING



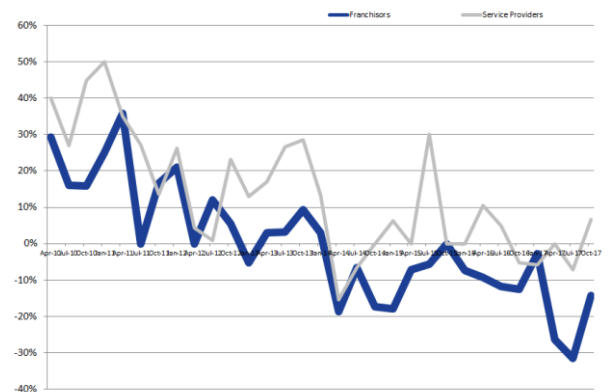
ACCESSTO SUITABLE FRANCHISEES



ACCESSTO SUITABLE LOCATIONS



ACCESSTO SUITABLE STAFF



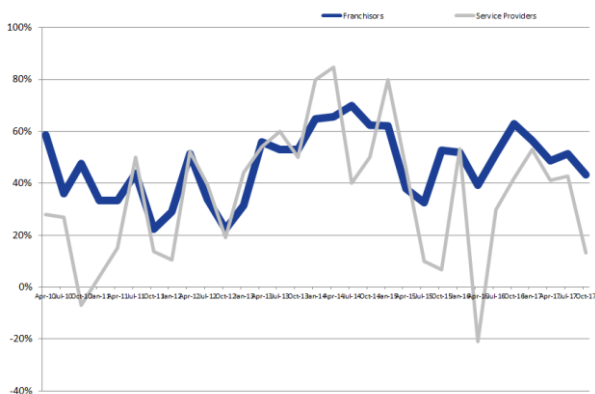
Franchisors sentiment toward the **availability of suitable staff** saw a positive increase at a net negative 14%, up from an all-time low of net negative 32%. Service Providers were equally positive up from net negative 7%, to net 7%. Finding suitable staff has always been a challenging area, however in this instance it is one of the only areas where positive gains (albeit still remaining net negative) are evident.

The Franchisee Picture

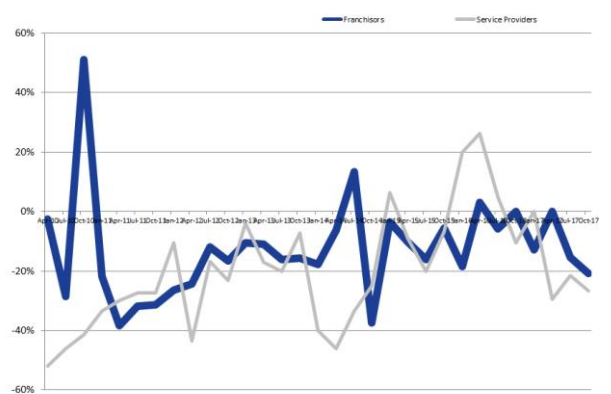
Despite more macro concerns, franchisor sentiment toward **franchisee sales levels** dipped although still remains strong at a net 43%, whilst Service Provider sentiment diminished from net 43% to a net 13%.

Franchisee operating costs, meanwhile, remain a challenge, with Franchisor sentiment declining for the second quarter from a net negative 15% to a negative 21%. Service Provider outlook remained more negative at a net negative 27% down from July's net negative 21%.

SALES LEVELS PER FRANCHISEE

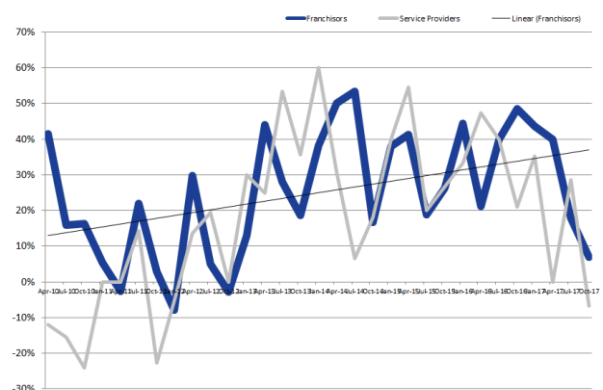


OPERATING COSTS PER FRANCHISEE



Finally, Franchisors sentiment towards **franchisee profitability levels**, which are a strong indicator of the economic climate took a dip for the second quarter to net 7%, down from a July net 18%. A very positive increase in July for Service Providers was reversed to net negative 7%; a drop of 36%.

FRANCHISEE PROFITABILITY LEVELS



Franchising Outlook

Franchisors were asked for qualitative responses on how things were looking in their sector. Sixteen useable responses were received with notable comments regarding uncertainty due to the local elections and the unknown impact of world changes. Positive comments tended to be industry specific with flattened, although still positive sales levels and a strengthening in availability of suitable staff and suitable locations. By contrast, less positive responses (often individual) included references to increased operating costs, finding franchisees, competition, legislative headaches, and the impact of an unknown Government.

The following examples were indicative of this sentiment:

- *Commercial Cleaning. Business as usual. Margins static, compliance driving up prices, hopefully this squeezes some bottom feeders out.*
- *Our sector is doing it tough at the minute. Our competitive landscape has never been so hard and the cost of raw materials is increasing.*
- *Furniture, vehicle repairs - Steady*
- *Higher costs and entry point levels will retard the growth of franchising, leasing costs will hopefully stagnate. Cost of fitout is a concern.*
- *Still going strong sales wise. Financing, costs etc could get worse due to change in Govt.*
- *Having difficulty finding suitable franchisees*
- *Sports retail - challenging at present*
- *A lot of uncertainty at the moment with the outcome of the election unclear - general comments relate to people not wanting to commit to business/investment until outcome is known*
- *Datamine figures for the last quarter show sales in the Cafes, Restaurants and Bars have started to slow down.*
- *Automotive Space very volatile and expecting the run of high growth to slow with the economy slowing*
- *Uncertainty of Govt will impact on our business revenue. Already feeling this although i doubt it will have a long term effect*
- *Retail sector- things have been tougher over the last 12 months compared to previous years that have been consistently up.*
- *Home Services. Decrease in number of franchisees and finance harder to get.*
- *Hospitality - looking ok but will be bumpy*
- *Commercial services. Anticipate general business to be about the same, possibly even softening a little bit.*
- *Overall conditions remain positive but unchanged. Premises and suitable franchisees remain a challenge but unchanged.*

Service Providers were similarly asked how they thought things were looking for franchisors and franchisees. Their responses also focused on domestic government uncertainty, but also added more macro concern – including the potential for world war. Some comments also referenced a slowdown in some sectors. Key examples include:

- *Same, same. The main issues for NZ business are externally driven, such as the World Economy, the threat of a widespread war. Over the last thirty years we have survived major economic challenges. SME owners find a way through - It's the big businesses that fail. Most of business in NZ is SME and so I think things are looking okay for the franchise sector.*
- *Present political uncertainty about next government & policies makes prediction difficult. In short term, maintenance of status-quo seems most likely scenario until new directions set.*
- *Over the next 12 months there is a lot of uncertainty both globally and domestically (including the NZ election). This makes it very difficult to comment on the above.*
- *Not too bad at all. Whichever party Winston decides to appoint as government and the deal he strikes could however impact.*
- *Much the same but I anticipate interest rates will rise a little and eat into profitability but not a lot*
- *Franchise sales enquiries are currently slower, as they always are around election time - similar dynamic to house sales. Once the election result is known, we expect a small surge before Christmas then more as people come back to work.*
- *Sales growth across a number of industries are showing signs of slowing down*
- *Very positive and helped by very impressive Survey results recently.*

Concluding Comment

Franchise Consultants' Franchising Confidence Index in October 2017 shows the impact of local and worldwide uncertainties, with caution being exercised. Additionally, both franchisors and service providers make note of declining demand, in some sectors. And franchisors, in particular, make many references to increased investment and operating costs, as well as competitive, compliance, franchisee recruitment and financing pressures.

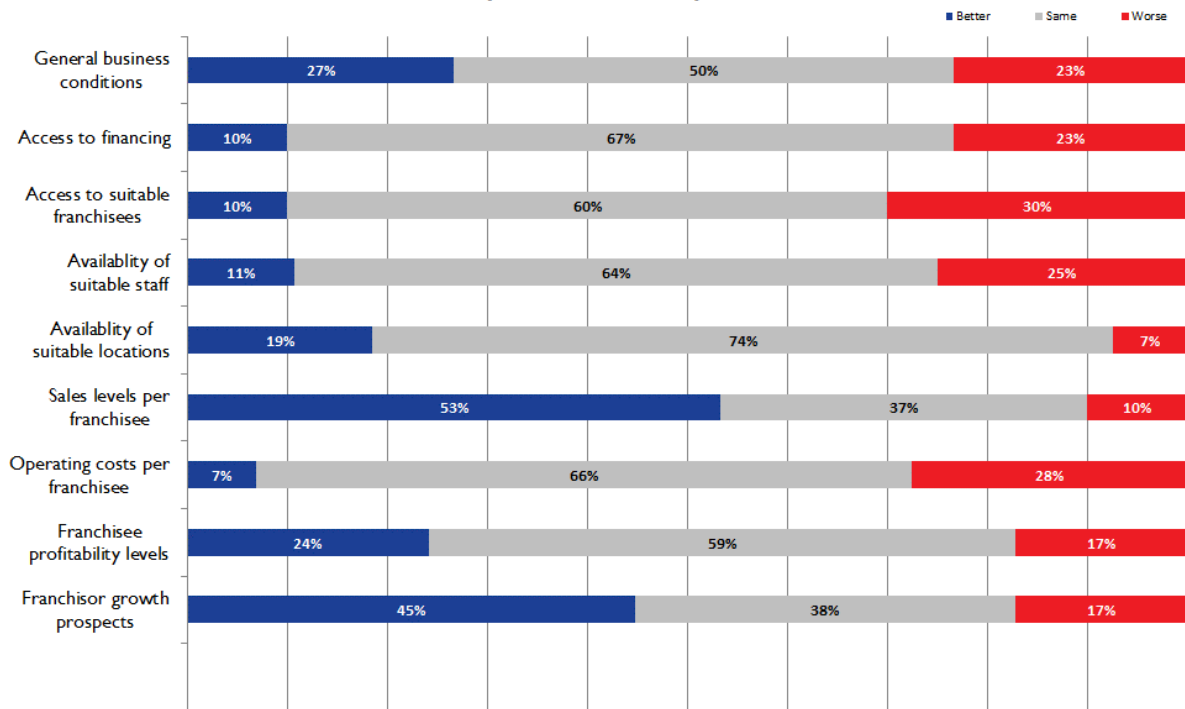
Particular note is given to uncertainty associated with the domestic election. Accordingly, we reference indicators during previous election years (notable 2011, and to a lesser degree, 2014) that saw similar dips in general business confidence. These proved temporary, with rapid gains in following quarters.

Increasingly, as indicated in the wider business press for business generally, franchisors need to take an active role in adapting and future-proofing their franchise systems – in an environment with many forces of change, like employment, technology, competition, access to capital, legislation, and as is currently seen; the government.

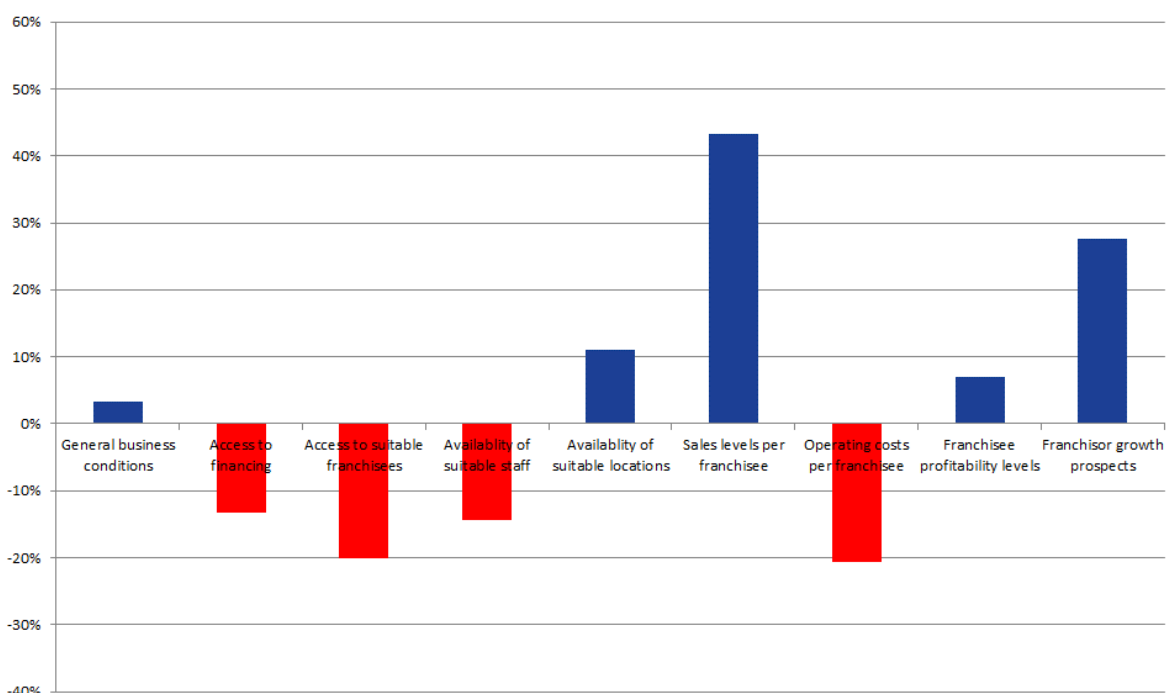
FRANCHISING CONFIDENCE CHARTS

The following four illustrations present individual and net Franchisor and Service Provider expectations (separate charts) for the following year across all questions, including general business conditions and franchisor growth prospects (covered above).

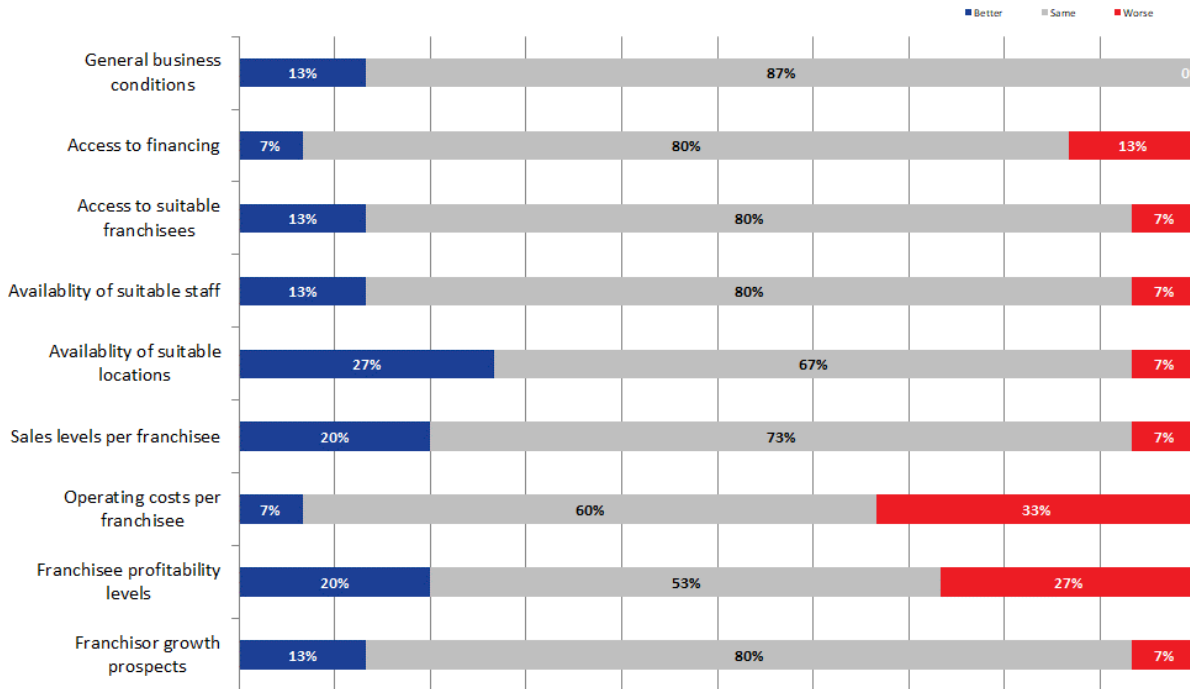
FRANCHISOR EXPECTATIONS (next 12 months)



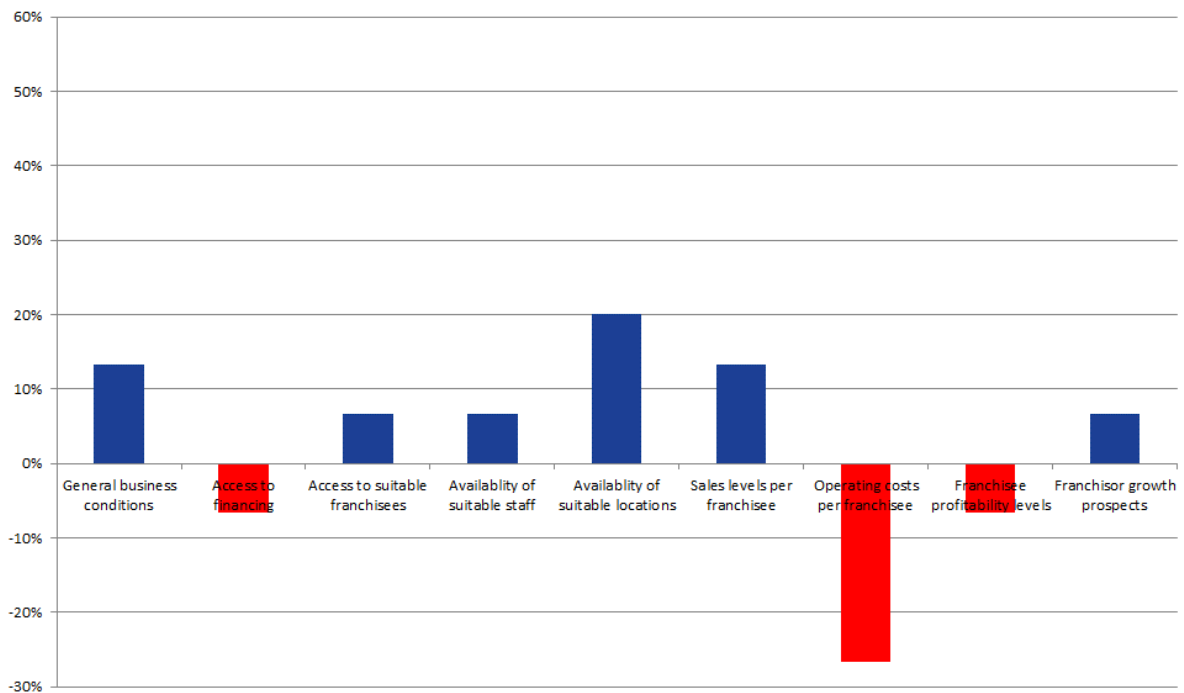
NET FRANCHISOR EXPECTATIONS



SERVICE PROVIDER EXPECTATIONS (next 12 months)



NET SERVICE PROVIDER EXPECTATIONS



Franchising Confidence Index

The Franchising Confidence Index represents the views and expectations of franchising, an important domain of business within the New Zealand economy.

Franchising is a substantial and growing domain of business making up an important part of the New Zealand economy. The *Franchising New Zealand 2012* survey, conducted by Massey University in collaboration with Griffith Business School, indicates New Zealand has 446 individual franchise systems comprising some 22,400 units (owned mostly by franchisees). The survey also suggests local franchise systems employ some 100,000 people. Finally, local expert estimates of total franchise system turnover range from \$15 to \$25 billion – suggesting franchising is a strong contributor to New Zealand GDP – as it is around the world. Companies involved in franchising are as diverse as Foodstuffs (New World, PAK'nSAVE, Four Square), NZ Post, Fisher & Paykel, Contact Energy, McDonald's, Columbus Coffee, Fastway Couriers, Harcourts and Fletcher Building.

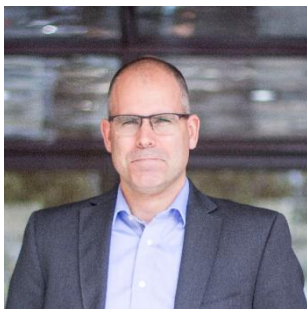
The Franchising Confidence Index represents confidence in key measures critical to the success of franchising in this country by reporting attitudes toward general business conditions, as well as key franchising growth determinants including access to capital, suitable potential franchisees, staff and locations. The Franchising Confidence Index also covers franchising health attributes and outcomes by exploring franchisee sales, operating costs and profitability, and franchise system growth prospects.

The data and analysis presented represents the views of 30 Franchisors and 15 Service Providers collected between Monday 2 October and Friday 13 October 2017. Findings from both groups are reported separately.

Respondents were asked whether they expected conditions to be 'better,' 'same' or 'worse.' 'Net' confidence is the difference between those reporting 'better' and 'worse.'

The results were compiled by Kayleen Smith, Business Support Manager, Franchise Consultants.

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Thinking of improving the results of an established franchise network? Franchise Consultants have had great success improving established franchising and licensing network performance for all stakeholders.