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## Creative Ways of Finding Finance in the Crunch

By Julie Bennett

**D**uring the worst credit crunch in decades, franchise companies have been finding creative ways to open new units.

While banks are expected to lend \$6.7 billion to U.S. franchises this year, it would take \$10.1 billion in lending to fully fund newcomers who want to start franchised businesses and existing franchisees who hope to expand, according to FRANdata, a research firm in Arlington, Va.

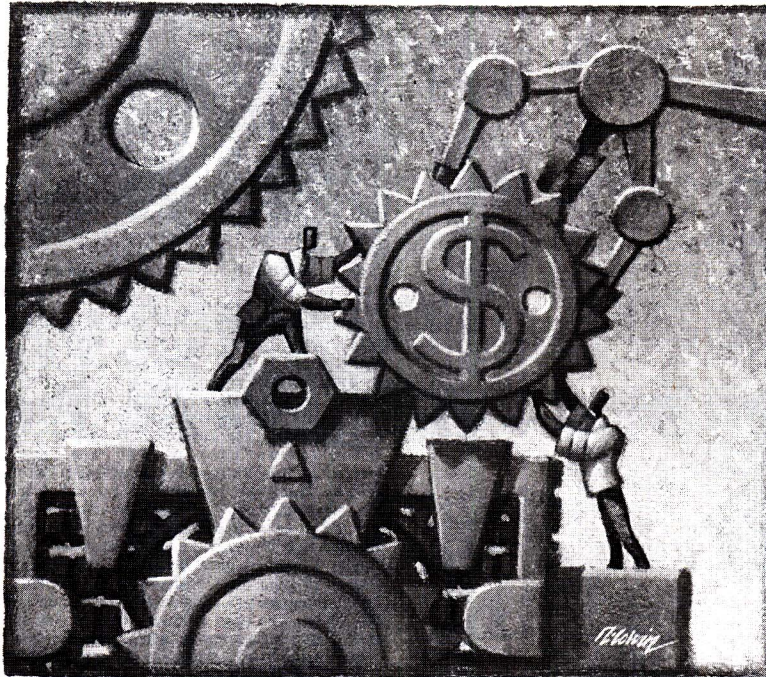
Ron Feldman, CEO of the Siegel Financial Group in Bala Cynwyd, Pa., says many franchisers are working with individual franchisees, to help shore up their credit, find additional investors or provide lenders with some kind of guarantee — the franchiser will take over the business if the franchisee gets into trouble, for example.

But others, like Showhomes, in Nashville, Tenn., are acting like banks themselves. Matt Kelton, chief operations officer, says, "When lending became so tight, we started financing half our franchise fee ourselves." Mr. Kelton plans to launch 25 franchises this year, to new franchisees who can put down \$15,000 and pay Showhomes the other \$15,000 over three years, plus 12.5% annual interest.

At least half of new franchisees take advantage of the financing, including George Hart of Denver, Colo., a retired military officer who borrowed \$24,000 from Showhomes to purchase two territories. "I felt the terms were good and I wanted to get started quickly to take advantage of the real estate rebound," Mr. Hart says. Showhomes franchisees supply luxury homes with home managers who move in with their own furniture. Franchisees collect a small monthly fee from the home managers, plus half of one percent of the list price when the house is sold. "I have a lot of home manager candidates now," Mr. Hart says, "who are good people caught in a bad situation. I just moved a man into an 8,000-square-foot, \$3.2 million mansion — and he had to put some of his furniture into storage."

### Varied Financing

Mr. Kelton says Showhomes turned to self-financing because banks are especially adverse to making business loans under \$100,000. Volvo Rents, in Asheville, N.C., finances franchisees for the opposite reason — starting a franchise that leases light to medium construction and industrial equipment like excavators, compressors and backhoes is too expensive for traditional lenders. Nick Mavrick, vice president of marketing, says Volvo, headquartered in Brussels, uses its finance company, Volvo Financial Services, to



lend \$4 million or more to qualified franchisees at an interest rate that fluctuates around 2% over Libor (London interbank offered rate).

Franchisee David Evans of Oklahoma City says he and his business partners looked at several equipment rental companies and the financing package was a main reason they chose Volvo. "We opened Jan. 4," Mr. Evans says, "and eventually we'll have \$5 million to \$7 million worth of fleet. Volvo's financing allows us to buy equipment as soon as our customers request it."

Some franchisers have enlisted their vendors to help finance new franchisees. Wireless Zone, based in Middletown, Conn., a cell phone retailer with 400 locations, finances half the \$30,000 franchise fee, plus another \$20,000 for signs and fixtures; service provider Verizon finances up to \$25,000 of each new store's buildout. Although franchisees have three years to pay off the notes, at 12% interest, most pay them off in the first year, says Sean Fitzgerald, vice president of franchise development. "We try to minimize upfront expenses for our franchisees, so they can use their capital to grow their businesses," says Mr. Fitzgerald.

Chris Jourdan of Newburgh, Ind., and his

partners used the financing packages to open their first three Wireless Zones; then reinvested their profits to open six more in Indiana, Kentucky and Ohio. "Sales are improving month after month," Mr. Jourdan says, "and we plan to keep opening more stores."

Other franchisers are building businesses around equipment franchisees can provide financing on their own. Scott Novis, CEO and founder of GameTruck in Tempe, Ariz., says he designed his portable video game franchise so that franchisees could purchase its most expensive elements — a high-end trailer and a truck to pull it — with "straightforward, asset-backed loans."

### Retirement Funds

Alan Cherry of Hummelstown, Penn., for example, put down \$20,000 on a trailer to house the parties he hosts for children ages eight to 12 and financed the rest through the trailer company. He used savings and cashed in retirement funds to buy a used truck, to pay his \$33,000 franchise fee and to equip the trailer with flat-screen monitors, a very long couch and dozens of multiplayer games. Mr. Cherry charges parents

\$295 for a two-hour party for up to 16 children and figures he needs to book five parties a week to make a profit. "Moms love it," he says, as do the kids.

Before the recession, many franchisers had strong relationships with national banks or non-bank lenders that would finance their franchisees. Today, most national lenders have ceased their franchise programs and prospective franchisees must turn to local banks. The problem, says FRANdata President Darrell Johnson, is that most of the country's 8,000 community banks have no experience with franchising. "Franchisees must help them feel comfortable with their concept and convince them that the franchisee will be around for the eight or so years required to pay back the loan," Mr. Johnson said.

Rod Marcotte, senior vice president of Christian Brothers Automotive Corp. in Houston, for example, talked several times to lending officers at Insouth Bank in Brownsville, Tenn., before they would lend \$260,000 to a new franchisee — even though the franchisee's family had banked there for three generations. "I told them how a Christian Brothers repair shop would be a good fit for the community," Mr. Marcotte says.

Franchisee Wes Pannel, who opened his shop in Jackson, Tenn., on March 1, says he met many times with the bank's president and loan officers. "I took some of them to Memphis to see a Christian Brothers shop that was already open," Mr. Pannel says, "and they spent time on my site watching the traffic go by before they approved the loan."

And before the lending crunch, loans guaranteed by the Small Business Administration were the mainstay of franchising. But SBA loan guarantees have fallen 37% from 2007 levels. R.J. Krone, startup support manager for Spring-Green Lawn Care Corp. in Plainfield, Ill., says, "We routinely used SBA-guarantees when it was easier." To help its franchisees, Spring-Green recently formed a partnership with Mr. Feldman's Siegel Financial Group, which is one of a handful of brokers that shop loans to SBA-affiliated lending institutions around the country. "Siegel prescreens each prospective franchisee," Mr. Krone says, "and lets us know if they're viable."

On paper, new Spring-Green franchisee Rick Locke of Indianapolis was more than viable. "My credit score is about 800, I have plenty of capital in savings and equity in my house," Mr. Locke says. "I thought getting a loan would be a no-brainer." But after his local bank turned him down, Mr. Locke signed on with Siegel last September. His loan, for \$117,000 from Wells Fargo Bank, finally closed on Dec. 31. Adds Mr. Locke: "If I saw such a challenge in obtaining a small business loan, what is happening to other talented people without a franchiser to help them?"