

**Franchise Business Economic Outlook**

**Prepared for**

**The International Franchise Association  
Educational Foundation**

**January 7, 2009**

---

PricewaterhouseCoopers has exercised reasonable professional care and diligence in the collection, processing, and reporting of this information. However, the data used is from third party sources and PricewaterhouseCoopers has not independently verified, validated, or audited the data.

PricewaterhouseCoopers makes no representations or warranties with respect to the accuracy of the information, nor whether it is suitable for the purposes to which it is put by users.

PricewaterhouseCoopers shall not be liable to any user of this report or to any other person or entity for any inaccuracy of this information or any errors or omissions in its content, regardless of the cause of such inaccuracy, error or omission. Furthermore, in no event shall PricewaterhouseCoopers be liable for consequential, incidental or punitive damages to any person or entity for any matter relating to this information.

---

# FRANCHISE BUSINESS ECONOMIC OUTLOOK

## TABLE OF CONTENTS

	<u>PAGE</u>
EXECUTIVE SUMMARY .....	E-1
I. INTRODUCTION.....	1
II. OUTLOOK FOR FRANCHISED BUSINESSES .....	2
III. BACKGROUND DATA.....	7
IV. FRANCHISE BUSINESS LEADER SURVEY.....	10
APPENDICES	
A. COMPOSITION OF FRANCHISE BUSINESS LINES .....	A-1
B. BUSINESS FORMAT AND PRODUCT DISTRIBUTION FRANCHISES.....	B-1

## FRANCHISE BUSINESS ECONOMIC OUTLOOK

### EXECUTIVE SUMMARY

This report provides the first franchise business economic outlook, a forecast of franchise activity by 10 business format lines for 2009. The forecast of franchise activity builds on previous studies by PricewaterhouseCoopers identifying the significant level of franchising in the United States.<sup>1</sup> This report was commissioned by the International Franchise Association Educational Foundation ("the Foundation").

#### A challenging year ahead

In its 2008 study on the economic significance of franchising, PwC reported that business format franchises operated 773,435 establishments in the United States in 2005, counting both establishments owned by franchisees and establishments owned by franchisors.<sup>2</sup> Franchised businesses provided 9 million full-time and part-time jobs and generated \$665.3 billion of output (the gross value of goods and services produced) for the national economy.

PwC's updated analysis presented in this report finds that between 2005 and 2007 franchised businesses continued their steady growth in number of establishments, employment, and economic output. By 2007, the number of establishments reached 847,246, which provided over 9.8 million jobs and generated \$816 billion in output.

The recession, which began in December 2007, is expected to continue into the middle of 2009, which would make it the longest recession since the Great Depression.<sup>3</sup> The onset of the current financial crisis and global recession, the most severe economic downturn since the early 1980s, will have a negative impact on franchise business growth. After years of steady growth, PwC estimates that franchise business growth slowed in 2008 and is likely to decline in 2009.

After posting a 2.1 percent increase in the number of establishments in 2008, PwC forecasts that the number of franchise establishments will decline by 1.2 percent in 2009 to 854,511 units (a loss of 10,273 units). Franchised businesses experienced a small reduction in jobs in 2008 (0.2 percent). PwC estimates a larger reduction in 2009 (2.1 percent)--resulting in a loss of 207,000 jobs between 2008 and 2009. Economic output contributed by franchised businesses grew by 2.8 percent in 2008. PwC estimates a decline of 0.5 percent in 2009--a loss of \$4.2 billion in 2009 (see **Table E-1**).

---

<sup>1</sup> PricewaterhouseCoopers LLP, *Economic Impact of Franchised Businesses* (February 24, 2004) and *Economic Impact of Franchised Businesses, Volume II: Results for 2005* (January 29, 2008).

<sup>2</sup> This report does not include estimates for product distribution franchises such as automotive and truck dealers, gasoline service stations, and beverage bottlers. In contrast, previous PwC reports included both product distribution franchises and business format franchises. For a definition of these two types of franchises see Appendix B.

<sup>3</sup> *Blue Chip Economic Indicators*, December 10, 2008.

**Table E-1 - Franchise Business Economic Outlook, 2006-2009**

	Annual percent change					
	2006	2007	2008	2009	2007/2008	2008/2009
Establishments	808,275	847,246	864,784	854,511	2.1%	-1.2%
Employment (Thousands)	9,473	9,805	9,785	9,578	-0.2%	-2.1%
Output (Billion of dollars)	\$742.5	\$816.0	\$839.2	\$835.0	2.8%	-0.5%

Source: PricewaterhouseCoopers.

Because franchised businesses are an integral part of the U.S. economy, they are by no means immune from the current financial crisis and global recession. The unfolding credit crunch has adversely impacted all businesses, including franchised businesses. According to a recent study by FRANdata, borrowing by franchises will fall by about 27 percent in 2009 compared to 2008, thus limiting the expansion of existing franchises as well as the entry of new franchises.<sup>4</sup>

The adverse impact of the current recession will have different effects on growth in establishments, employment, and output within each franchise business line (see **Table E-2**).

- **Establishments.** While most business format lines are estimated to experience net reductions in the number of establishments, franchised Quick Service Restaurants and Table/Full Service Restaurants are projected to experience a net increase in establishment units in 2009.
- **Employment.** All business lines, except the two restaurant business lines, are forecast to reduce employment in 2009. The Quick Service and Table/Full Service Restaurant business lines are projected to increase employment by 0.4 percent and 0.2 percent respectively. The three business lines projected to experience the largest percentage reductions are Automotive; Retail Food; and Retail Products and Services--each contracting employment by more than five percent.
- **Output.** Output is forecast to decline in eight out of the 10 lines of business. The three business lines projected to see the largest percentage contraction are Lodging; Business Services; and Real Estate. The Quick Service and Table/Full Service Restaurant business lines are expected to increase output in 2009.

<sup>4</sup> FRANdata, *2009 Franchise Capital Requirement Estimate* (November 2008). FRANdata, founded in 1989, is a research and information services firm specializing in franchising industry data. FRANdata is also the exclusive contractor for the Small Business Administration (SBA) Franchise Registry.

**Table E-2 - Franchise Business Economic Outlook by Business Line, 2009**

Business Lines	Establishments		Employment (Thousands)		Output (Billions of dollars)	
	Amount	Percent change over prior year	Amount	Percent change over prior year	Amount	Percent change over prior year
Automotive	36,563	-1.5%	178	-5.8%	\$36.0	-0.4%
Commercial and Residential Services	59,461	-3.5%	326	-4.1%	\$42.6	-1.3%
Quick Service Restaurants	182,136	1.5%	3,361	0.4%	\$190.0	2.4%
Table/Full Service Restaurants	46,650	1.3%	1,081	0.2%	\$61.1	2.2%
Retail Food	66,228	-2.0%	829	-5.8%	\$66.7	-0.4%
Lodging	32,202	-2.6%	661	-4.9%	\$63.6	-3.2%
Real Estate	37,735	-3.2%	153	-4.2%	\$24.7	-2.1%
Retail Products and Services	82,681	-2.1%	561	-5.8%	\$49.6	-0.7%
Business Services	217,861	-2.5%	1,365	-3.9%	\$173.1	-2.8%
Personal Services	<u>92,994</u>	-0.2%	<u>1,063</u>	-1.5%	<u>\$127.7</u>	-0.8%
<b>Total</b>	<b>854,511</b>	<b>-1.2%</b>	<b>9,578</b>	<b>-2.1%</b>	<b>\$835.0</b>	<b>-0.5%</b>

Source: PricewaterhouseCoopers.

### Franchise business leaders remain cautiously optimistic

While the U.S. economy is expected to continue to struggle in 2009, many franchise business leaders remain optimistic about the prospects for their own businesses. The results of the 2008 *IFA Franchise Business Leader Survey* suggest that franchise business leaders foresee both challenges and opportunities in the coming year.

Franchisors are employing a number of strategies to deal with the current economic downturn, including tightening budgets and cutting overhead costs. Yet, the survey shows that franchisors also look to the entrepreneurial spirit of franchisees and the fundamentals of the franchise business model as factors that will help them “weather the economic storm.” Strikingly, while only 24.6 percent of survey respondents believe that the economy will do better in 2009 than in 2008, 49.1 percent believe their own businesses will do better in 2009.

## FRANCHISE BUSINESS ECONOMIC OUTLOOK

### I. Introduction

This report presents the first franchise business economic outlook by PricewaterhouseCoopers ("PwC") for the International Franchise Association Educational Foundation ("the Foundation"). Previously, PwC has quantified the economic significance of franchised businesses in the United States for the Foundation. These economic impact studies found that franchised businesses are one of the largest employers in the country providing millions of American jobs and generating hundreds of billions of output in the U.S. economy.<sup>5</sup>

This report projects key national-level economic measurements of business format franchising into 2009. The report does not include estimates for product distribution franchises such as automotive and truck dealers, gasoline service stations, and beverage bottling. (For a description of the differences between product distribution and business format franchises, see Appendix B.) Section II presents PwC's economic outlook of franchising at the national level for 10 business lines in which franchising is prevalent, namely:

- Automotive
- Commercial and Residential Services
- Quick Service Restaurants
- Table/Full Service Restaurants
- Retail Food
- Lodging
- Real Estate
- Retail Products and Services
- Business Services
- Personal Services

For each of the 10 business lines, the projections include forecasts for 2009 (and estimates for 2006-2008) of:

- Franchise establishments (both company-owned and franchisee-owned)
- Franchise employment (positions filled by part-time and full-time employees or by self-employed individuals)
- Franchise output (the gross value of goods and services produced, a concept that is comparable to sales for most industries)

Section III describes the key data used in preparing the franchise business economic outlook, including the latest macroeconomic outlook prepared by Inforum and data on franchising establishment units collected by FRANdata.<sup>6</sup> This section also provides a comparison of the projections of franchised business economic activities from this report with other recently released forecasts for a few selected lines of businesses.

Section IV summarizes the findings of a recent franchise business leader survey conducted by the IFA Educational Foundation.

---

<sup>5</sup> PricewaterhouseCoopers LLP, *Economic Impact of Franchised Businesses* (February 24, 2004) and *Economic Impact of Franchised Businesses, Volume II: Results for 2005* (January 29, 2008).

<sup>6</sup> Inforum, established in 1967, is an economic education and research organization housed at the University of Maryland that specializes in the development and use of Interindustry-Macroeconomic (IM) models that combine input-output structure with econometric equations in a dynamic and detailed framework.

## II. Outlook for franchised businesses

### A. Overall outlook

PwC forecasts declines in establishments, employment, and output for franchise businesses in 2009, after experiencing broad growth from 2005, the last period covered by PwC's previous estimates.

PwC has previously estimated that in 2005 business format franchises operated 773,435 establishments in the United States, counting both establishments owned by franchisees and establishments owned by franchisors.<sup>7</sup> Business format franchises provided 9 million full-time and part-time jobs and produced \$665.3 billion of output in 2005.<sup>8</sup>

PwC's updated estimates show that the number of business format franchise establishments continued to grow from 2005 through 2008 (to 864,784 units). PwC estimates that establishments will decline by 1.2 percent in 2009 to 854,511 units (a loss of 10,273 units). Employment in business format franchises is estimated to have peaked in 2007 at 9.8 million. In 2008, business format franchises are estimated to have posted a small reduction in employment (0.2 percent). PwC forecasts a larger drop in 2009 (2.1 percent) to bring the number of jobs in business format franchises to 9.6 million. This represents a decline of 20,000 jobs between 2007 and 2008, and an additional decline of 207,000 between 2008 and 2009.

Economic output generated by business format franchises grew 2.8 percent in 2008. PwC estimates output will decline by 0.5 percent (\$4.2 billion) in 2009 (see **Table II-1**, below).

**Table II-1 - Franchise Business Economic Outlook, 2006-2009**

	2006	2007	2008	2009	Annual percent change	
					2007/2008	2008/2009
Establishments	808,275	847,246	864,784	854,511	2.1%	-1.2%
Employment (Thousands)	9,473	9,805	9,785	9,578	-0.2%	-2.1%
Output (Billion of dollars)	\$742.5	\$816.0	\$839.2	\$835.0	2.8%	-0.5%

Source: PricewaterhouseCoopers.

<sup>7</sup> An establishment is a single physical location at which business is conducted or services or industrial operations are performed. A business may consist of more than one establishment. An establishment may be owned by the franchisor or the franchisee.

<sup>8</sup> Jobs are positions filled by part-time and full-time employees or by self-employed individuals. The output of a business is the gross value of goods and services it produces. It is a concept that is comparable to sales for most industries. In government input-output accounts, the output of goods-producing industries is measured by the value of shipments. For most other industries, output is measured by receipts or revenues from goods and services sold. A special case is the output of the wholesale and retail industries, which is measured generally as the difference between receipts or revenues and the cost of goods sold--this difference is referred to as "margin".

## B. Outlook by business line

To place the 2006-2009 projections in context, we first report the number of establishments, employment, and output by the 10 business format lines of business in 2005, as previously estimated by PwC in its 2008 report (**Table II-2**).

Business lines with the largest number of establishments in 2005 were Business Services; Quick Service Restaurants; and Retail Products and Services. Employment was greatest in Quick Service Restaurants; Business Services; and Table/Full Service Restaurants. Output was greatest in Quick Service Restaurants; Business Services; and Personal Services.

**Table II-2 - Establishments, Employment and Output by Business Format Lines, 2005**

<b>Business Lines</b>	<b>Establishments</b>	<b>Employment (Thousands)</b>	<b>Output (Billions of dollars)</b>
Automotive	35,616	176	\$25.3
Commercial and Residential Services	54,495	314	\$32.9
Quick Service Restaurants	167,578	3,153	\$152.1
Table/Full Service Restaurants	42,285	1,046	\$50.4
Retail Food	61,039	779	\$47.0
Lodging	30,014	570	\$48.0
Real Estate	33,900	155	\$26.3
Retail Products and Services	78,621	538	\$36.5
Business Services	193,063	1,348	\$150.7
Personal Services	<u>76,824</u>	<u>938</u>	<u>\$96.1</u>
<b>Total</b>	<b>773,435</b>	<b>9,017</b>	<b>\$665.3</b>

Source: PricewaterhouseCoopers LLP, *Economic Impact of Franchised Businesses, Volume II: Results for 2005* (January 29, 2008).

**Establishments by business line: 2006-2009**

**Table II-3** shows projected franchise establishment units by the 10 business format lines for the 2006-2009 period. PwC estimates that nine of the 10 franchise business lines experienced continuous growth in establishments between 2005 and 2008, with only Real Estate declining between 2007 and 2008. Between 2008 and 2009, growth in establishments is expected in only two of the 10 business lines--Quick Service Restaurants and Table/Full Service Restaurants.

Franchised businesses in Real Estate are projected to suffer a net reduction in unit counts of 4.0 percent and 3.2 percent in 2008 and 2009, respectively, bringing the 2009 unit count in Real Estate franchises nearly back to 2006 levels. Other lines of businesses projected to experience large percentage reductions in unit counts in 2009 include: Commercial and Residential Services; Lodging; Business Services; and Retail Products and Services.

Overall, the number of establishments in business format franchises is projected to decline by 1.2 percent in 2009.

**Table II-3 - Franchise Establishments by Business Lines, 2006-2009**

Business Lines	Establishments				Annual percent change	
	2006	2007	2008	2009	2007/2008	2008/2009
Automotive	36,341	35,695	37,126	36,563	4.0%	-1.5%
Commercial and Residential Services	56,742	60,268	61,632	59,461	2.3%	-3.5%
Quick Service Restaurants	171,183	177,499	179,366	182,136	1.1%	1.5%
Table/Full Service Restaurants	44,058	45,836	46,033	46,650	0.4%	1.3%
Retail Food	63,392	65,377	67,584	66,228	3.4%	-2.0%
Lodging	30,858	31,003	33,056	32,202	6.6%	-2.6%
Real Estate	37,564	40,577	38,965	37,735	-4.0%	-3.2%
Retail Products and Services	79,450	82,104	84,434	82,681	2.8%	-2.1%
Business Services	207,807	219,638	223,377	217,861	1.7%	-2.5%
Personal Services	<u>80,879</u>	<u>89,248</u>	<u>93,211</u>	<u>92,994</u>	4.4%	-0.2%
<b>Total</b>	<b>808,275</b>	<b>847,246</b>	<b>864,784</b>	<b>854,511</b>	<b>2.1%</b>	<b>-1.2%</b>

Source: PricewaterhouseCoopers.

**Employment by business line: 2006-2009**

**Table II-4** shows the projected franchise employment by 10 business format lines of business for the 2006-2009 period. PwC estimates that most business format franchises experienced a steady increase in employment through 2007. The current recession caused a reduction in employment in 2008 for all business format franchises except for those in Commercial and Residential Services and Personal Services. In 2009, all business format franchises, except for those in Quick Service Restaurant and Table/Full Service Restaurant business lines, are projected to further reduce employment.

The largest percentage reductions in employment in 2009 are expected for franchises in Automotive; Retail Food; and Retail Products and Services. In each of these three business lines the number of full-time and part-time jobs is expected to decline by more than 5 percent. Other franchise business lines that are projected to reduce their employment by between 4 and 5 percent are: Lodging; Real Estate; and Commercial and Residential Services.

Overall, business format franchises are projected to reduce their employment by 2.1 percent in 2009.

**Table II-4 - Franchise Employment by Business Lines, 2006-2009**

Business Lines	Employment (Thousands)				Annual percent change	
	2006	2007	2008	2009	2007/2008	2008/2009
Automotive	183	195	189	178	-3.0%	-5.8%
Commercial and Residential Services	343	339	340	326	0.3%	-4.1%
Quick Service Restaurants	3,308	3,372	3,347	3,361	-0.7%	0.4%
Table/Full Service Restaurants	1,083	1,093	1,079	1,081	-1.3%	0.2%
Retail Food	829	901	880	829	-2.3%	-5.8%
Lodging	615	666	695	661	4.4%	-4.9%
Real Estate	159	164	160	153	-2.3%	-4.2%
Retail Products and Services	567	611	595	561	-2.5%	-5.8%
Business Services	1,387	1,423	1,420	1,365	-0.2%	-3.9%
Personal Services	999	1,043	1,079	1,063	3.4%	-1.5%
<b>Total</b>	<b>9,473</b>	<b>9,805</b>	<b>9,785</b>	<b>9,578</b>	<b>-0.2%</b>	<b>-2.1%</b>

Source: PricewaterhouseCoopers.

**Output by business line: 2006-2009**

**Table II-5** shows the projected franchise output by 10 business format lines of business for the 2006-2009 period. Most business lines experienced growth in output each year between 2005 and 2008. The only exception is Real Estate (with a peak in output prior to 2005). The three business lines with the largest percentage increases in output in 2008 were Personal Services; Lodging; and Automotive.

For 2009, PwC projects contractions in output for eight out of the 10 business format lines. The three business lines with the largest percentage declines in output in 2009 are forecast to be Lodging; Business Services; and Real Estate. Output is projected to increase in the Quick Service Restaurants and Table/Full Service Restaurants business lines, in large part due to menu price inflation.

Overall, annual output by business format franchises is projected to decline by 0.5 percent in 2009.

**Table II-5 - Franchise Output by Business Lines, 2006-2009**

Business Lines	Output (Billions of dollars)				Annual percent change	
	2006	2007	2008	2009	2007/2008	2008/2009
Automotive	\$29.8	\$34.7	\$36.1	\$36.0	4.2%	-0.4%
Commercial and Residential Services	\$38.5	\$41.7	\$43.2	\$42.6	3.6%	-1.3%
Quick Service Restaurants	\$169.8	\$184.0	\$185.5	\$190.0	0.8%	2.4%
Table/Full Service Restaurants	\$55.6	\$59.7	\$59.8	\$61.1	0.2%	2.2%
Retail Food	\$55.6	\$64.9	\$67.0	\$66.7	3.1%	-0.4%
Lodging	\$54.7	\$62.0	\$65.8	\$63.6	6.1%	-3.2%
Real Estate	\$26.0	\$26.0	\$25.2	\$24.7	-2.9%	-2.1%
Retail Products and Services	\$42.3	\$48.6	\$49.9	\$49.6	2.7%	-0.7%
Business Services	\$161.7	\$173.7	\$178.0	\$173.1	2.5%	-2.8%
Personal Services	<u>\$108.6</u>	<u>\$120.8</u>	<u>\$128.6</u>	<u>\$127.7</u>	6.5%	-0.8%
<b>Total</b>	<b>\$742.5</b>	<b>\$816.0</b>	<b>\$839.2</b>	<b>\$835.0</b>	<b>2.8%</b>	<b>-0.5%</b>

Source: PricewaterhouseCoopers.

### III. Background Data

PwC's franchise business economic outlook is developed based on the latest macroeconomic and industry forecast prepared by Inforum; franchise establishment data provided by FRANdata; and PwC's analysis of historical relationships between franchised businesses and the rest of the U.S. economy.

#### A. Macroeconomic outlook

The U.S. economy is in the midst of the most severe recession since the early 1980s. In the latest economic outlook by Inforum (released on December 9, 2008), Inforum anticipates a continuation of the sharp downturn well into 2009 and a very sluggish recovery from the recession. GDP is expected to contract through the first part of 2009 and growth in the latter part of the year is expected to be weak. On an annual basis, every demand component of GDP falls except for government expenditure and net exports. Given lower housing and financial wealth and anticipated further layoffs, consumers will continue to retrench into 2009--private consumption spending is expected to fall by 1.6 percent, causing retail sales to drop, with cascading adverse impacts on a broad range of sectors of the economy, including franchised businesses. Household savings rates are projected to rise. The increase in household savings reduces consumption, thus prolonging and exacerbating the current recession (see **Table III-1**).

**Table III-1 - Macroeconomic Outlook, 2007-2009**

	<u>Actual</u> <u>2007</u>	<u>Estimate</u> <u>2008</u>	<u>Forecast</u> <u>2009</u>
Nominal GDP (Billions of dollars)	13,807.5	14,300.0	14,193.0
Nominal GDP (Percentage change)	4.8	3.6	-0.7
Real GDP (Percentage change)	2.0	1.4	-1.3
Real PCE (Percentage change)	2.8	0.3	-1.6
Real Gross Private Fixed Investment (Percentage change)	-5.4	-5.3	-8.5
Real Net Exports (Percentage change)	-11.2	-30.5	-15.3
Real Government Expenditures (Percentage change)	2.0	2.8	2.1
GDP Price Index (Percentage change)	2.7	2.2	0.6
PCE Price Index (Percentage change)	2.6	2.6	0.0
Employment (In millions)	150.1	147.8	145.0
Employment (Percentage change)	1.1	-1.5	-1.9
Unemployment Rate (Percent)	4.6	5.8	7.6
Three-Month Treasury Bill Rate (Percent)	4.4	1.4	0.5
10-Year Treasury Note Rate (Percent)	4.6	3.7	3.0
Personal Income (Percentage change)	6.1	2.8	0.7
Personal Savings Rate (Percent)	0.6	1.7	4.9

Source: Inforum, December 9, 2008.

Inforum expects the outlook for government spending to be highly uncertain. While federal spending is likely to continue growing, there will be noticeable slowing of defense spending as the recent buildup of defense investment comes to an end. State and local government also are hit hard by the recession and face greatly increased budgetary pressures to curtail spending and investment. On monetary policy, the Federal Reserve already cut rates substantially in 2008 and Treasury interest rates have fallen to levels not seen in many years.

Even with a substantial stimulus package underway, Inforum expects some five million jobs to be lost between 2007 and 2009. Inforum projects the unemployment rate to rise sharply in 2009.

Overall, Inforum expects U.S. real GDP to fall by 1.3 percent in 2009 from its 2008 level, while the unemployment rate is expected to hit close to 8 percent in 2009.

**Key macroeconomic assumptions**

Inforum's macroeconomic and industry forecasts are determined by the relationships embodied in its economic model and the assumptions for key exogenous variables. Over the short run, various cyclical factors, such as interest rates and employment growth, international issues such as trading partner growth, oil prices, and exchange rates, or monetary and fiscal policy, can exert significant influences over the outlook. The following describes the key assumptions supporting the current Inforum economic outlook:

1. **Housing markets:** Inforum expects home prices to decline further in 2009 as the subprime mortgage disaster continues to unfold.

2. **Fiscal stimulus:** Inforum has assumed an economic stimulus package that (1) is large--\$650 billion over three years; (2) focuses on infrastructure development (highways, bridges, retrofitting government building for energy efficiency, etc.); (3) includes tax cuts of modest amounts directed at middle-income taxpayers; (4) includes enhanced payments to persons (transfer payments) for unemployment insurance, food stamps, veterans benefits, and the like; and (5) includes some immediate spending on "green" technology (see **Table III-2**).

**Table III-2 - Assumed Economic Stimulus Package**  
[Amount in billions of dollars]

<b>Category</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>Total</b>
Tax cuts to persons	90	70	60	220
Transfer payments to persons	26	28	28	82
Investments in green technology	12	15	15	42
Infrastructure investment	<u>78</u>	<u>114</u>	<u>114</u>	<u>306</u>
<b>Annual Total</b>	<b>206</b>	<b>227</b>	<b>217</b>	<b>650</b>

3. **Monetary policy:** Inforum assumes that the Federal Reserve will hold the federal funds rate at low levels, causing the 3-month Treasury bill rate to average 0.5 percent in 2009. Inforum further assumes that the Federal Reserve will fulfill its "lender of last resort" function by implementing additional "quantitative easing" in the coming year.

4. **Energy prices:** Inforum expects the annual domestic refiner acquisition price to average \$98 per barrel in 2008, followed by a sharp decrease to \$66 in 2009. It expects the wellhead price for natural gas to average \$6.7 per thousand cubic feet in 2008 and fall to \$5.7 in 2009.

**5. International considerations:** The Inforum forecast incorporates information from its Bilateral Trade Model (BTM). BTM is a linked system of country models, in which countries are linked to one another through trade flows at the commodity level. As such, the international variables for the U.S. model are not strictly exogenous. For example, faster growth in the United States, say, from a cut in tax rates, generally raises the demand for imports. When these results are incorporated in the international system, foreign-country exports and foreign-country GDP will be raised. In turn, faster growth in these countries increases U.S. exports and alters the composition of U.S. final demand. It should be noted that the United States is not the only country having a recession. Before the National Bureau of Economic Research (NBER) formally announced the United States was in a recession, Japan, Germany, France, and the United Kingdom all had made similar announcements. In fact, 12 of the 13 countries in Inforum's International System will have negative rates of growth in 2009.

#### **B. Franchise establishment counts**

Macroeconomic models such as the Inforum models do not typically provide estimates on the number of business establishments. To calibrate the franchise unit estimates for this report, PwC has used historical franchise establishment data collected by FRANdata. FRANdata maintains an extensive database of information about the companies that franchise, the brands they manage, and the franchisees who invest in those brands. The principal source of this information is the Franchise Disclosure Documents (FDDs), formerly known as Uniform Franchise Offering Circulars (UFOCs).

Franchisors are required under Federal and State regulations to provide FDDs to prospective franchisees prior to the sale of a franchise. Certain states require FDDs to be filed and approved by state regulators before the franchisor is allowed to sell franchises within the state. These disclosures provide prospective franchisees with information describing various aspects of the franchise program. The FDD also provides a set of the franchisor's audited financial statements and a copy of each form or contract a prospective franchisee is expected to sign in order to buy a franchise. The 23 sections of the disclosure cover such things as franchisee's initial investment, initial franchise fees and other costs, the franchisor's litigation history, restrictions on and obligations of the franchisee and franchisor, financing arrangements, earnings claims, and a list of existing franchised locations.

#### **C. Other reference data**

As a point of reference, PwC's complete projection of all 10 lines of business format franchise activities can be compared to specialized projections for individual lines of businesses. For example, in the latest issue of PwC's *Hospitality Directions* (November 2008), a research journal for the U.S. lodging industry, it is projected that industry revenues will grow by 1.6 percent in 2008 before declining by 4.2 percent in 2009. For the franchised segment of the lodging industry, PwC's analysis in this report (Table II-5, above) projects stronger revenue growth in 2008 (6.1 percent) and a less severe reduction in revenues for 2009 (-3.2 percent).

Another reference point is provided by the National Restaurant Association (NRA) annual forecast for the restaurant industry. Although there are differences in how the NRA defines the restaurant segments, their latest forecast (released on December 19, 2008), projects an increase in Quick Service Restaurant sales of 4.0 percent in 2009 and a 1.0 percent increase in Full Service Restaurant sales. Sales at eating and drinking establishments are projected to increase by 2.2 percent in 2009. After adjusting for inflation, the NRA projects an overall decline in sales of 1.0 percent for the restaurant industry in 2009. PwC's analysis for the franchise segment of the industry is for a 2.4 percent increase in nominal sales for Quick Service Restaurants in 2009 and a 2.2 percent increase in sales for Table/ Full Service Restaurants.

#### IV. Business Leader Sentiment Survey

In November 2008, the International Franchise Association (IFA) conducted the first *IFA Franchise Business Leader Survey*.<sup>9</sup> This short survey was sent to 1,287 IFA member companies across all business lines and asked franchise business leaders about their views on the general economic outlook for 2009, as well as the prospects for their own businesses in the year to come. In addition, survey respondents were asked to rank the issues that will be most important for them in the coming year. The IFA received 167 responses (a response rate of 12.9 percent) representing a cross-section of industry leaders. The statistical significance of the results is difficult to judge and it would not be accurate to generalize about the IFA membership as a whole based on the survey results. For example, only eight percent of the respondents were in the quick service restaurants business line, while 20 percent of IFA's membership is in that business line. The survey responses, however, do provide an interesting snapshot of franchise business leaders' sentiment. In addition, a number of the survey questions were similar to questions asked on IFA's May 2008 Member Survey,<sup>10</sup> which provides an opportunity to examine how sentiment changed over the course of 2008.

#### Key Results

While the U.S. economy is expected to continue to struggle in 2009, franchise business leaders remain somewhat optimistic about the prospects for their own businesses. The results of the 2008 *IFA Franchise Business Leader Survey* suggest that franchise business leaders foresee both challenges and opportunities in the coming year. While many franchisors are tightening budgets, cutting overhead costs, and implementing other strategies to deal with the economic downturn, others look to the entrepreneurial spirit of franchisees and the fundamentals of the franchise business model as factors that will help them "weather the economic storm." Compared to the May, 2008 IFA Member Survey, franchise business leaders are considerably less optimistic about current and future business conditions. Despite this fact, many survey respondents still expect to see increases in same store sales, employment, and units.

Question	Better	Worse	About the Same
Do you expect the U.S. economy to be better in 2009 than in 2008?	24.6%	43.7%	31.7%
Do you expect your company's U.S. business to do better in 2009 than in 2008?	49.1%	15.0%	35.9%

Source: *IFA Franchise Business Leader Survey*, November 2008.

- Nearly half (43.7 percent) of survey respondents believe that the U.S. economy will do worse in 2009 than in 2008, while only 24.6 percent believe the economy will do better in 2009.
- Despite these numbers, 49.1 percent of survey respondents indicated that they expected their own business to do better in 2009 than in 2008. An additional 35.9 percent expected their businesses to do about the same over the next year.

<sup>9</sup> The survey was distributed by email to IFA members on November 11, 2008, with a deadline for responding of November 19, 2008. For a copy of the survey questions see Appendix B.

<sup>10</sup> The member survey was sent to more than 11,000 individuals in May 2008. 450 responses were received.

The overall business conditions for my business at the present time are:		
	May 2008 Survey	November 2008 Survey
Very Good	22.5%	16.8%
Somewhat Good	27.4%	22.2%
About Average	30.1%	21.0%
Somewhat Poor	18.0%	31.1%
Very Poor	2.0%	9.0%

Looking ahead to the next 12 months, do you believe the overall economic conditions for your business will be:		
	May 2008 Survey	November 2008 Survey
Very Good	24.3%	13.8%
Somewhat Good	31.4%	25.1%
About Average	28.5%	23.4%
Somewhat Poor	14.5%	33.5%
Very Poor	1.3%	4.2%

Source: IFA Member Survey, May 2008 and IFA Franchise Business Leader Survey, November 2008.

- Compared to the May, 2008 IFA Member Survey, franchise leaders' opinions on the current and future business conditions are considerably less optimistic. Only 16.8 percent of respondents said the current business conditions faced by their company are "very good," compared to 22.5 percent in the May 2008 survey. Over the same period, the percent of respondents who felt that current business conditions were "somewhat poor" increased from 18.0 percent to 31.1 percent. In November, 9.0 percent of respondents said that current business conditions were "very poor," up from just 2.0 percent in May.
- Similarly, the percent of respondents who felt business conditions over the next 12 months would be "very good" fell from 24.3 percent in May to 13.8 percent in November, while the percentage of respondents who felt future business conditions would be "somewhat poor" rose from 14.5 percent to 33.5 percent. In November 2008, 4.2 percent of respondents believed that business conditions will be "very poor" over the next 12 months, compared to just 1.3 percent in May 2008.

Question	Increase Significantly (by 6 percent or more)	Increase moderately (by less than 6 percent)	Decrease moderately (by less than 6 percent)	Decrease Significantly (by 6 percent or more)
How do you expect your company's U.S. same store sales (both company owned and franchisee owned) in 2009 to compare to same store sales in 2008?	24.6%	43.7%	25.7%	6.0%
Does your company expect to increase or decrease its number of units/franchises in operation in the U.S. during 2009?	40.1%	45.5%	12.6%	1.8%
How do you expect your company's U.S. employment in 2009 to compare to its employment in 2008?	18.6%	52.7%	25.7%	3.0%

Source: IFA Franchise Business Leader Survey, November 2008.

- Between May and November of 2008, franchise business leaders lowered their expectations for growth in system-wide same store sales for 2009. While 39.8 percent of respondents to the May survey predicted significant increases in 2009 same store sales (increases of 6 percent or more), only 24.6 percent now believe same store sales will grow by 6 percent or more in 2009.

- Nearly half (43.7 percent) of survey respondents now expect moderate sales growth (growth of less than 6 percent), while 25.7 percent of survey respondents believe that their same-store sales will decrease moderately.
- Interestingly, franchise business leaders have not significantly reduced their expectations for unit growth. Over 85 percent of survey respondents expect to see unit growth in 2009 (40.1 percent of respondents expect significant increases while 45.5 percent expect moderate growth).
- In addition, survey respondents expect to see modest increases in their companies' employment in 2009. More than half (52.7 percent) of respondents expect employment to increase by less than 6 percent. In contrast only 28.7% of respondents expect to see a decrease in their employment.

### Key Issues for Franchisors in 2009

In addition to questions on current and future business conditions, survey respondents were asked to rank the top five issues for their businesses over the next 12 months, with "1" being the most important issue and "5" being the least important of the top 5 issues. The table below summarizes the responses.

What are the top 5 issues for your business over the next 12 months?						
Issue	Number of Respondents Ranking Issue:					Response Count
	1	2	3	4	5	
Business Climate	57	35	25	14	10	141
Financing/Credit Crunch	50	33	27	10	8	128
Franchise Sales/Development	42	32	18	20	13	125
Underperforming Franchisees	20	22	19	28	20	109
Competition	4	11	21	13	30	79
Government Regulations	4	10	13	11	9	47
Gas Prices	6	5	15	10	9	45
International Development	5	5	9	11	14	44
Labor Shortages/Workforce Issues	3	9	9	9	9	39
Legal Concerns	5	3	8	14	8	38
Minimum Wage	6	4	5	13	9	37
Health Care	3	5	10	10	8	36
Education	6	8	8	5	5	32
Franchise Legislation	3	8	10	5	6	32
Other						8

Source: IFA Franchise Business Leader Survey, November 2008.

According to the survey, the top three issues facing franchise businesses over the next 12 months, in terms of the total number of responses, are (1) the business climate, (2) the financial crisis/credit crunch, and (3) franchises sales and development.

### *Business Climate*

The current economic downturn is affecting all businesses, including franchises. As discussed above, franchise business leaders are less optimistic about the business conditions they will face over the next 12 months than they were in May of 2008. The deterioration of the economy, lagging consumer confidence, and tight credit markets are cause for concern among franchise business leaders.

According to one survey respondent, "The dramatically low levels of consumer confidence have impacted our clients' willingness to move forward with ... projects. Our franchisees have to work harder than ever to try to keep generating sales."

However, while survey respondents foresee a tough year ahead many remain cautiously optimistic about their own businesses. As one franchisor put it, "While I believe the economic outlook is grim, I think that there is a great opportunity for franchisors to grow their business."

Some franchise executives point to the underlying strength of the franchise business model and the entrepreneurial spirit of franchisees as factors that will help "weather the economic storm" while others are stepping up marketing efforts and implementing other strategies to help deal with the economic downturn.

### *Financing/Credit Crunch*

Many survey respondents point to the ongoing financial crisis as another major cause for concern in the year ahead. The credit crisis is likely to result in further reductions in conventional lending to franchised businesses.

As one survey respondent put it, "With almost no banks willing to lend, franchisors are faced with tremendous growth challenges in 2009 as few new franchisees will be able to sign on without help from a lender. Current franchisees are faced with the same issues as some see their essential bank credit-lines being withdrawn." As a result, many franchisors have had to reduce their planned unit growth for 2009.

### *Franchise Sales/Development*

As a result of the credit crunch many franchisors are worried about franchise sales and development. There are other factors that suggest 2009 may be a tough year for franchise unit growth. In a tough business environment, some entrepreneurs may be hesitant to start new businesses. According to one survey respondent, "The credit crunch and sluggish economy combined with a situation in which existing units that would otherwise have been profitable and now may fail (because of the economy) has created a general lack of optimism and a less favorable environment for opening new units."

### *Other*

A number of the top concerns of franchise business leaders can be grouped together under the general heading of government regulation and legislation. Government regulation, minimum wage, health care, and franchise legislation combine for a total of 152 responses. Other important issues facing franchises in 2009 include underperforming franchisees, competition, education, and international development.

## Summary

The current economic downturn has adversely impacted all businesses, including franchised businesses. The *IFA Franchise Business Leader Survey* illustrates that while franchisors are concerned about business conditions, they remain cautiously optimistic about the future.

This optimism is based on franchisors' strong belief in the underlying strength of the franchise business model. According to one survey respondent, "Franchised businesses have a tendency to withstand economic conditions longer than most mom/pop or non-franchised businesses because they have a proven model of success." Others point to the entrepreneurial spirit of their franchisees, saying "Franchised businesses will do generally well as the owner operators have drive and stake and a say in their own operations and businesses." Other respondents said they see opportunities even in times of economic uncertainty. As one put it, "Times like these are when the next wave of innovators will stake their claims."

While respondents pointed to a "tough year" ahead, many said that they are tightening budgets, cutting overhead costs, and implementing new strategies to "minimize the damage through strategic and tactical planning with support services to franchisees" such as increased marketing, improved technology systems, and programs to help prospective franchisees find financing. As a result, the surveyed franchise business leaders seem optimistic about their ability to "weather the economic downturn."

## **Appendix A**

### **Composition of Franchise Business Lines**

This report covers the following 10 lines of business format franchising.

1. **Automotive**  
Includes motor vehicle parts and supply stores, tire dealers, automotive equipment rental and leasing, and automotive repair and maintenance
2. **Commercial and Residential Services**  
Includes building, developing, and general contracting; heavy construction; special trade contractors; facilities support services; services to buildings and dwellings; and waste management and remediation services
3. **Quick Service Restaurants**  
Includes limited-service eating places, cafeterias, fast-food restaurants, beverage bars, ice cream parlors, pizza delivery establishments, carryout sandwich shops, and carryout service shops with on-premises baking of donuts, cookies, and bagels
4. **Table/Full Service Restaurants**
5. **Retail Food**  
Includes food and beverage stores, convenience stores, food service contractors, caterers, and retail bakeries
6. **Lodging**  
Includes hotels, motels, and other accommodations
7. **Real Estate**  
Includes lessors of buildings, self-storage units, and other real estate; real estate agents and brokers; and property management and other related activities
8. **Retail Products and Services**  
Includes furniture and home furnishings stores, electronics and appliance stores, building material and garden equipment and supplies dealers, health and personal care stores, clothing and general merchandise stores, florists and gift stores, consumer goods rentals, photographic services, and book and music stores
9. **Business Services**  
Includes printing, business transportation, warehousing and storage, data processing services, insurance agencies and brokerages, office administrative services, employment services, investigation and security services, tax preparation and payroll services, and heavy equipment leasing
10. **Personal Services**  
Includes educational services, health care, entertainment and recreation, personal and laundry services, veterinary services, loan brokers, credit intermediation and related activities, and personal transportation

## Appendix B

### Business Format Franchises and Product Distribution Franchises

In the *Economic Impact of Franchised Businesses, Volume 2*, PwC provided estimates of the number of establishments, jobs, payroll, and economic output for both business format franchises and product distribution franchises.

Business format franchises are more prevalent than product distribution franchises. For example, in 2005, there were 773,456 business format franchise establishments and 135,817 product distribution franchise establishments (see **Table B-1**).

Product distribution franchises sell the franchisor's products and are for the most part supplier-dealer relationships. The franchisor licenses its trademark to franchisees but typically does not provide them with a "system" for operating their business. Typical product distribution franchises are automotive and truck dealers, gasoline service stations, and beverage bottling.

Business format franchises, including the business lines described in this report, not only use a franchisor's product, service, and trademark but also operate the business under a method established by the franchisor. This method of operation, described as a business format, often includes marketing plans, training, advertising, and operations manuals.

**Table B-1 - Establishments, Employment, Payroll and Output in Business Format and Product Distribution Franchises, 2005**

	Business Format Franchises	Product Distribution Franchises
Establishments	773,436	135,817
Employment	9,017,267	2,011,938
Payroll (in \$billions)	206.9	71.7
Output (in \$billions)	665.3	215.6

Source: PricewaterhouseCoopers LLP, *Economic Impact of Franchised Businesses, Volume II: Results for 2005* (January 29, 2008).