Male Speaker: Welcome to the REI Diamonds Show with Dan Breslin, your source for real estate investment, Jewels of Wisdom.

Dan Breslin: Bob Bernotas, welcome to the REI Diamond Show. How you doing today, Bob?

Bob Bernotas: Thank you, Dan. Great to be here.

Dan: Nice. For the audience who does not know, they probably know from the title that we select... I'm sure that you'll have to do with franchising businesses. Some of the listeners will remember some of our other past discussions around why real estate investors specifically might be interested in the franchise as an option to supplement to cash flow and things of that nature. Before we dive in and pull apart that piece of the topic, tell me, Bob, how did you arrive at your place in life now as a franchise consultant?

Bob: Oh, my goodness. I've been a franchise investor, owner operator since 1986. I've owned multiple franchise concepts and multiple units with each that I've built and sold over the years. Some with a great deal of success and some not with as much success. Also, was CEO of a national chain and I've been consulting, I guess for a couple decades now. Originally, I was consulting mostly on the franchise side, helping companies position for growth over the last 10, 12 years, have morphed exclusively onto the franchisee side, helping people or groups find the right franchise fit, help them acquire financing for that and help them move forward.

Dan: We were talking before the show started and I mentioned West Coast Video. I wonder if some of our listeners remember that place.

Bob: They're going to need to be the older ones, but hey, everybody knows what happened in that industry. Not around anymore, but yeah, that was my foray into franchising. December of 1986, opened my first West Coast Video franchise on Wayne and Shelton Avenues in Germantown.

Dan: Nice.

Bob: Just by pure luck in terms of the draw and getting the right location, that unit opened in December, that January it was the top unit in the chain, which allowed me to propel into a number of other units with that chain and got me started in franchising.

Dan: That's pretty cool. Yeah. I know a lot of our listeners, I'm sure some of them own property right now on Wayne or Shelton Avenue for sure. If not, they recognize the intersection in Philadelphia. You exited that business, I think, if I remember from my research before the show, you exited that one successfully, right? What year was that?

Bob: I did. I sold my last West Coast Video, I think it was 1991. I stayed in the industry for a while longer on the consulting basis, and I actually developed a number of independent video stores and worked with some investors and had partial ownership in a bunch of them up and down the eastern seaboard. Then technology started to take over and finally executed that industry.

Dan: Did you see that coming? Were you guys in the industry well, aware of what was going on and sort of making the exit on time?

Bob: Yeah. The threat was hanging around so long and there were so many rumors and so much information out there, but it was never seemed to come to fruition. So, you started to ignore it, right? But finally it did. Fortunately, I got out at a fairly decent time. I wish I got out a year or two earlier, but I still did pretty well with it.

Dan: Nice. Nice. How important is timing in the franchise world? So, I was doing some other research on franchise businesses in general, and one of the concerns that this gentleman was writing about, the blog post I think I saw, was when a hot franchise comes to market, let's say it's exercise, it's Orange theory. I forget if that was 10, 15 years ago. They've obviously done well. We do have this, I guess, macro trend of fitness in general happening in the United States and has been for a while where that's a growing industry and it's been trending. But maybe you could tell me it's like how many fitness businesses are out there in the franchise world, and is that a good idea? And are there some that are kind of going to franchise explode and then sort of fall back? And maybe how does the listener avoid a risk of something like that, if that's [crosstalk]

Bob: Yeah, look, there's some good fitness type franchises. Most of them I think would fall in the boutique fitness category like in Orange theory. I think you'll find that there's a proliferation of them in my opinion. There's too many of them. You're absolutely right. When it comes to timing, in terms of the types of franchises to get into. The dirty little secret in the franchise world is that if you don't get in at the right time, all right, usually the opportunity's over. When you start hearing about a brand and you're hearing about it, because it's probably already come to your marketplace and there's not an opportunity to acquire it any longer, and the brands that really have strong economic models, franchise investors recognize it.

They're tipped off by people like me. My franchise investor clients, I let them know right away. Typically, those brands get bought up pretty quickly. The issue is it shuts out a lot of other people that would love to get into the brand, but just all the real estate is bought up very rapidly. I'll give you an example. I bought a franchise about four and a half months ago, I think it's been, and this just happened because I had a local client I was working with, about 45 minutes from me. I showed him a number of brands. I showed him this brand. He absolutely fell in love with it. He just didn't have the capital to execute upon it, and he was just trying to target one unit. I raised my hand and said, I love this brand, I'll invest with you.

He was open to that and what was going to be one unit quickly became three units. I brought in a couple other people, put together a little investment group, and we did six units. The only problem we had was, me being into west of the Philadelphia area, everything sold out too fast. Meaning we had to go two hours northeast into Central Jersey to buy locations, to buy territory because there was nothing else available around me. But that brand from introduction, once it got into the portfolio of a really strong FSO that helped it grow and they just started franchising, I think it was 2022, I want to say 2023. It might have been beginning of 2023, but they got into the portfolio of a group that is helping them grow, eight months the country is virtually sold out. There's almost nothing left. So, when you have a brand with a real strong economic model, especially if it's a sexier brand, that's a men's health type brand, and it's a reasonably priced brick and mortar goes into office space, not retail. So, to build out reasonable 3, 325 and that, that range to get open. But when you see a brand like that, with that type of unit economics, it tends to sell out e exceedingly fast.

Dan: If we could pull in the thread, because I know I'm curious on deal structures and financing, and I know the audience is too, so 325 grand to open location, we're talking about six. So, it's a total of like 1.8 to 1.9 million. For those six units, is there some component that is debt, or is that going to be you and the investors all through in the cash and there's no debt?

Bob: Yeah, we did a cash deal on that one.

Dan: Okay. All right.

Bob: Typically, debt-wise, there's so many different instruments that are available in franchising and it's not like starting an independent business on your own and you go to the bank and hey, what's your operating history? You don't have any at that point. Most of these, at least the ones that I work with, the franchise companies, they're SBA approved, so getting SBA lending is not usually a challenge. Typically, they're looking for about 20% capitalization and you can borrow the rest.

Dan: So that means 20% down borrowing from SBA is the small business administration.

Bob: Correct.

Dan: What are those interest rates right now, Bob?

Bob: You don't want to know. They're high.

Dan: Well, I think we do. We're all into the real estate business and we're all thinking real [crosstalk]

Bob: Ten, 11%. It's high. [Crosstalk] It's a 10-year term. I always counsel my clients, look, pay it off as soon as you can. Two years, three years, four years to be done with the interest. There's [crosstalk]

Dan: Are they adjustable rate loans?

Bob: Yeah, they are.

Dan: So, they may go down if rates were to cool off?

Bob: Correct.

Dan: Okay. All right.

Bob: Correct.

Dan: So, somehow though, Bob, because I know a lot of people on the call, if you told them, hey, you got to buy a four-unit apartment building with 20% down and you have to pay 10 to 11%, it just kills the deal. It doesn't work at all.

Bob: Yeah, I get it. Yeah.

Dan: Is that the case right now in franchising, or are deals working even in light of those interest rates?

Bob: No, they're working and the reason being, because there's so many other possibilities. A lot of people will use, if they have some property, they'll leverage the property home equity loans. There's something called a 401(k) rollover or Robs program which is heavily used in franchising, but it allows you to roll funds from your 401(k) or an IRA into a business. You have to do it under a certain structure, but without taxation, without penalty, without interest so you don't have an interest.

Dan: Wow. I know a lot of the listeners are probably familiar with self-directing the 401(k)s, and one of the rules in a self-directed IRA is you're not allowed to invest in your own business. That's why I think you're alluding to a special structure with this rollover.

Bob: Correct. Yeah. I work with a, a number of entities. There're three main entities who provide most of the financing to the franchise industry. Each of them you know, do these programs, but you have to roll it into a C corporation. They will help you get that set up. You pay a fee up front for them to set that all up for you, and then you're paying some monthly fee, 120 bucks or so per month, and they do all the filings and whatnot to make sure that you stay in compliance.

Dan: We touched on you exiting West Coast Video. If somebody were to do the 401(k) rollover into a C Corp bank, and then sell that business later because it's profitable, they can make their money, they don't want to manage it, whatever the case is, how does that unwinding of that scenario look?

Bob: Typically, you're going to do an asset sale, you're not going to sell the corporation. That's a great question. I wish I knew the answer. I don't want to give you misinformation on that.

Dan: Okay.

Bob: I never did the 401k rollover myself. A lot of my clients have, the ones that have, because it's a newer program, they haven't exited at this point. So I can't answer that question.

Dan: Got you. When did the program come out? Do you know?

Bob: Oh, it, I think it's been around for about 10 years, I want to say. [Crosstalk]

Dan: Do you remember what was it if we tagged it to a president that was in office, I assume somebody along the way had this idea and pushed it through with their administration, maybe?

Bob: I don't know. That's a great question though.

Dan: It does make sense, right? The 401(k) rollover, we self-direct. There are guys who are flipping real estate within their IRA, most of the people I know who are self-directing their IRA have two, $300,000 in there, put it in a self-direct, and then they're funding deals like mines. It's a fix and flood deal. I borrow 280,000 at 10%, two points. They love it. It goes all straight back into their IRA and then when the day comes for them to harvest the IRA, they're golden. It sounds like the government might have put this into place to encourage entrepreneurship. It obviously grows some employment and keeps the economy growing and rolling and it seems and feels like a good idea. But I know that the real estate audience is like, can I flip these businesses inside my IRAs, is that where we're getting?

Bob: Well, I'll tell you, with franchise investors, that's typically the strategy. Whether you go into this and you're thinking long term, this is a 20-year play with a franchise 10-year play. A lot of people go into it and it's a three-year, five-year play. With the units that we did, I talked to my investment group and our plan is to, hey, if somebody comes to us with a price, we are going to be willing to sell. With franchising, what I have recognized over the years, typically, if you decide to sell, you're going to see a three to five multiple of earnings.

Dan: Okay.

Bob: That's why I think franchising with the right companies is a good investment. Look, there's over 4,000 different franchises out there. Honestly, Dan, I wouldn't go near 60% of them. But then again, there's some really, really good ones out there. If you're realizing you start something for a couple of 300, $400,000 and you're able to drop a couple of 100k to the bottom line, so you have really nice cash flow, you decide to sell that in three years and it's throwing off a couple of 100 K to the bottom line, you should be able to sell that for somewhere between 600 to a million dollars.

Dan: You've got 300 or so in it.

Bob: Correct.

Dan: Okay. Yeah, I think that probably makes sense to a lot of real estate people, we understand the flipping of the asset. That would be like a long-term capital gains type of scenario because you're selling the asset, the business. So, it's a favorable way to make large chunks of capital over a course of time maybe.

Bob: What I like about this, real estate's obviously very, very safe. What I like about this, and if you pick the brand, it can be very, very safe as well. The equity builds so fast in this. If you drive that bottom line, I'll give you another example. The one that I bought, the unit economics that it is showing the average units of their corporate units, because they just didn't have a lot of operating franchises, they didn't have any that have reached a year. So, this is based on their corporate units, but typically a franchise runs more efficiently than corporate units. This is almost an immutable law of franchising to franchises outperform corporate units. In any event, but their corporate units were averaging 1.8 top line over 600 bottom line on an investment just three [crosstalk] But that's why this one sold out in eight months.

Dan: Got you. So, this becomes the hot brand, the cash flow becomes reliable. Even if it [crosstalk] would you expect that to grow from 600 in three years or like level off as cannibalization occurs?

Bob: I don't know, honestly, because look, the company launched in '18 and that was the company units that like, the first one launching in '18 to the latest one, it might have just over a year under its belt and the average of them. So, it's everywhere in between. It's not like these are five, 10-year-old units.

Dan: Yeah.

Bob: They reach those numbers pretty quickly.

Dan: Yeah. So, you got your money back anyway in the first year, and it's like the rest is in a sense, grief a little bit.

Bob: Yeah. In fact, the first unit, what they show in their franchise disclosure document or item 19 of their franchise disclosure document, that unit that opened the 2018 did 2.5 top line. It was over 900 bottom line, but they did it out of 889 square feet.

Dan: Wow.

Bob: So, look, I can't, tell you that that's normal in franchising. [Crosstalk] It is far from it. That is a unicorn. If someone says to me, if I'm working with a client and someone says to me, Bob, show me the best financial opportunities in franchising, ROI earnings, I don't give them what the widget is as long as it's ethical, provides value service to the community and what I mainly work in are semi passive franchises. There’re really three buckets of franchising. There is full-time franchises. You jump into it with both feet. You walk away from your corporate job, eventually that franchise is going to become semi-passive once systems are running smoothly and you have the right people in place. Then there's also the bucket of passive franchises. Things like car washes, automated car washes, laundromats, salon suite type concepts. Those tend to be more expensive. A million up to how many millions do you want to spend? The middle bucket is semi-passive franchises, where I try to really focus on, because you can find concepts, like I just mentioned to you, that men's health concept that are reasonably priced, you have to trade some time 10, 20 hours a week to start with. But it becomes less and less over time when systems are running smoothly and the right people are in place. So that's the bucket I feel most comfortable with and most of my clients are looking for.

Dan: Can you give me an idea, like a metric? Could we have like an exam. Let's say it's you, and I'm your client Bob, and I'm like, Bob, can you give me the idea of the ROI, let's say, I'm trying to consider, maybe I will go full time, but what will be the ROI on my three to 500,000? Or I'm like, hey Bob, I want the passive franchise. What's my ROI on the million bucks in a year and it's semi passive 500,000. Again, what's my ROI? So, is there an ROI metric that would be acceptable in your eyes being in the industry for so long?

Bob: Yeah. If you look at passive concepts, and I'll mention something like a salon suite concept, and let's say on average it's about a million-and-a-half dollars and you have no employees with that. Basically, you're renting, you're doing a beautiful build out in rented space, or you can buy the space and you're renting it to people in the beauty industry. They all have their little areas and it's a national call center. So, they're taking all the appointments and so forth. No employees few hours a week tops you're going to put into something like that. But your investment might be a million bucks, but having a 250, maybe $300,000 bottom line is reasonable with those concepts.

Dan: Wow. So that might be 20 to 30% ROI?

Bob: If you're looking at it on cash, on cash return and you're borrowing 80%, then it could be better. It could be in the 1oo% range.

Dan: Yeah. You're answering my question there is if that was like, bad news is I see 30%, it makes me think I'm in the wrong business and you're accustomed to getting much more like 200% on the men's health range.

Bob: If you get the right franchise, there's lots of franchises. Like I said, I would not go anywhere near. You could buy yourself a low paying job. Not to disparage companies like, well, I'm not going to disparage him. I don't want to get sued.

Dan: Yeah, I know which ones you're talking about.

Bob: It's a good concept. Stay away from food.

Dan: [Crosstalk] Yeah, yeah, for context Bob, where I was going with it is I own apartment buildings. I buy them for 600, 900,000 and we use a metric of yield on cost as like a safe way in this environment to figure out if we're making money.

Bob: Okay.

Dan: Yield on cost is what's the ROI on the total cost? I buy it for 600, I put 400, it's a million bucks. If my yield on cost is 10% there and there's 100K in ROI at the end of the day, that's probably a good deal depending on the neighborhood.

Bob: Yeah.

Dan: That number, as you get into 10 or 20 million-dollar buildings, that number may be 7 to 8% and someone's happy with that. So, as we go through the suite at 2 to 320%, I think there's some people listening like, man, that's phenomenal and that's Bob's least favorite. Could we touch on the ROI for like the semi-passive that sort of meets your hurdle and where you start to get excited for client?

Bob: Well, yeah, your return on investment's going to be a lot better, but you're going to trade some time. In your early stages, you might be putting in, let's say in the first six months, you might be putting 20 hours a week in, then it'll become less in the next six months should become less in the following six months. But with somebody, semi-passive models, either, it's a simple enough concept that you can manage it in that much time or it's a manage-to-manager model. One of the cool things about it is, especially if you get into the service category, non-brick and mortar retail category. Things that are, I'll give you an example. Like the home service category. People look at it, and often, they'll look down upon it like, well, that's a blue-collar industry. Do I really want to be in that? There's so much money in that category. What I'm seeing, and I'm really seeing over the last 10 plus years, it's a fragmented mom-and-pop industry ripe for rollup. You're seeing more and more franchise companies step into that space and take market share away from the moms and pops. But there's a few things that are driving it. The baby boomers were they do-it-yourself generation, they pretty much aged out of that, and the younger generations are,` not to disparage them, but most in the younger generations are, hey my time's too valuable. I'll hire somebody else to do that.

What's really driving it is younger people aren't getting into the trades anymore. It's leaving a void. So, there's a great opportunity in those types of franchises. What I find so interesting about it is the scalability of them. So, I'm looking at buying another franchise right now. I have a client, he's actually a friend of mine, I've been trying to help for about a year to find a franchise. Finally, he landed on one and he's absolutely in love with it. He's actually supposed to sign on Monday and I'm investing with him. But I don't know if you've heard of ADU's accessory dwelling units?

Dan: Oh, yeah.

Bob: Okay. Yeah. Well, this is the first franchise company that stick building ADUs. But the unit economic's off the charts on this one. The cost to get into it with a single franchise is sub 200K. I think they're showing, like in their FDD 15 to 185 is the range for a single franchise up and running. But they have two different models. They have an executive model, which is that semi-passive model, and they have a full-time model, two employees, project manager, and a salesperson, you start out with. If you're jumping into it full-time, you take on one of those roles, hire the other role. Company helps you hire the general contractor in your market. You start out with one, but as it scales, you will need more than that. You'll need another salesperson, you'll need another project manager. What I love about something like this is that if you buy a second franchise, you're just buying more dirt. You're doubling the size of your territory. If you buy a third franchise, you're tripling the size of your territory. So, the second franchise, I think, with that brand is 49.5. A third franchise, I think is 40.

We're looking at 10. We're mapping it out now, but we're looking to purchase 10 units with this concept. So, our investment is still going to be sub 500 K, but it gives us a huge, huge upside with it. So, scalability with these types of concepts is so much less expensive than when you're looking at brick and mortar. Orange theory, for instance. It's over a million-dollar investment, believe it or not. Most franchise owners own multiples of that concept. When you look at some of their numbers, what I saw published most recently, average top line, 1.1 average, bottom line around 200K, good investment.

Each one of those that you open, you might send another million dollars on each one. Whereas these types of concepts horizontal scaling is so inexpensive, but then there's also, and this is what I'm seeing with franchise investors now, there's the opportunity to vertically scale. You are in a service related business. Like I just placed somebody into a fencing franchise. Let's say a year, two years, three years down the road, they decide I want to get into another franchise because I'm getting so many requests for decking. They buy a decking franchise, they introduce that franchise to the same customer base that already knows and trusts their first brand. They're gaining economies to scale. Their cost of customer acquisition is going down.

Now what you're starting to see, Dan is franchise investors that were strictly relegated to brick and mortar, retail, food, fitness, things of that nature, beauty and putting a manager, opening one, putting a manager in place, opening another, putting a manager, opening a third, and then district manager, and then opening more. Those investors now seem to be migrating over to service-oriented businesses because more and more of those companies now have developed platforms to support franchisees on a semi-passive basis. They just are offering more tools. As an example, it might be a national call center. So, they take all the inbound inquiries from the marketing and advertising that you plug into, they convert that into an appointment for your salesperson as one example.

Dan: Okay. So, they're just booking the appointments and then your guy is showing up there. One of the biggest risks comes to mind for decking, maybe not as much fencing, but the ADUs especially, I'm like, oh my God, it's your general contractor risk. Right? It's like we flipped 331 houses last year and we got burned by contractors, like to the tune of six figures and we've done hundreds and hundreds and hundreds of deals over the year. Thousands of deals just more than a thousand in the last three years alone and we were burned. Maybe we weren't as strong on vetting the general contract. I'd be curious if you have any of the nuance or tips how they presented and addressed the general contractor risk.

Bob: Yeah. Well, they actually find a general contractor for you. Now look, I don't know how, it's a relatively new company. They've been around since same 2018, but they started franchising last year, but the unit economics that they're showing in their model, they own 10 territories, they're based in Sacramento, California. In 2022, the 10 territories that they own, when you look at their item 19, in their franchise disclosure document, it shows that they generated $49 million in revenue. For 2023, they added some more territories, but still most of the business was coming from those original 10. They did 88 million. But take those 10 divide by 49 million, they're looking at 4.9 million per territory. Now, the bottom line on that, I can't, I know what it is. I can't speak to it, but it's real solid.

Dan: Yeah, [crosstalk] Hey, you got a client, 49 in California, 4.9 million is probably 25 accessory dwelling unit. For anyone who doesn't know, that's like they're building a house in the backyard essentially as a method for solving the housing shortage. They're probably $200,000 a piece. I'm like just talking.

Bob: Exactly.

Dan: Yeah. [Crosstalk]. In Chicago, that economic may not actually work. You may not be able to get 200 grands for the accessory dwelling, but it's probably a much smaller unit in Chicago, just by nature of the size of the lot. We're talking about a garage with an apartment above it kind of. So maybe you're a hundred, I assume they probably have decent financing as part of that, you're getting to bring to the homeowner and say, hey, we have this 8% financing. You're going to rent out the ad unit backyard and it's going to be wonderful.

Bob: Correct. But their unit sizes are ranging from 220 square feet, if memory serves me correct. All the way up to a couple thousand. That's a house.

Dan: Yeah, no kidding.

Bob: But they do. To your point, you nailed it. Most, about 70% of what they're doing is on a property where a single-family home exists, whether it's attached to the home, it's detached to a home. They're stick building so they match the exterior [crosstalk] facade. Yeah. Right. To the home. So, it's not a modular that they just drop down. You're looking, looking at typically a six to seven month build. But most of that is, or a good portion of at least half is the permitting process. and everything that they do. They work with a national permitting company, so they handle all that upfront for you. They have a national call center. So, when you plug into their digital marketing, they're handling all those inbound calls and converting those into an appointment for your salesperson.

Dan: Yeah, that sounds nice. Just knowing my limited experience in Chicago, we're all excited about the ADU, right? I think there's plenty of inventory, but the areas are challenging, crime, that kind of thing. So, like the inventory to exist in the city of Chicago it's really tough to say that's the solution for the housing shortage. But you do have all these new zoning rules that have come out for the A DU, and this is going on nationally. I'm a member of the Urban Land Institute, and that's a development, I guess like a knowledge body if you'll, so Urban Land Institute is tracking green construction.

Anyway, where I'm going with that, Bob is the, ADU has been a popular topic around the real estate development community at the highest levels. Urban Land Institute also advises a lot of zoning boards and politicians and things of that nature. So, it's in a sense, a lobbying group to push things like green technology. Years ago, it was transit-oriented development, meaning building large apartments and condo buildings right there on the train tracks or within walking distance so as to reduce the number of cars that would be owned by the residents of those buildings. That was like a 10-year ago trend. I'd say that the ADU is like within the last five years has been one of the most talked about trends at the high level for the country. Especially it's gotten a lot more prominence and green light in a lot of districts push through for zoning as the housing shortage has gotten to new levels here.

Bob: Interesting. I should have you talk to my clients.

Dan: Yeah, well [inaudible] do that. and then as a [Crosstalk] Go ahead.

Bob: With the ADUs, what this company is showing is that about 70% of them are going onto a property with an existing home for grandma an aging parent, a kid coming home from college, in some cases, gyms, offices, pool houses. It could be attached to the house, it could be over garage, it could be a garage conversion. But about 30% are being bought by investors who are buying, in some cases, like lots around a lake or something, putting them on these lots and Airbnbing them.

Dan: Yeah. That's another trend. That one just from my view in the last year-and-a-half, the new construction development for Airbnbs and these little tiny homes, really interesting space. The one point on the Chicago zoning issue, it's interesting to hear you say that they have the National Permitting company, because one of the things with building the ADU is you're sitting here reviewing architectural plans, you're going back and forth to building, you're going through the permit department. Like that's a hassle. So, to do that for 24 projects, let's say you get in a year when you're up and running, sounds like a pretty cool value that the franchisor is bringing to the table there.

Bob: Yeah. Yeah. I would agree. I liked this organization

Dan: It's interesting too, hear you say that 70% is the existing home market from their $88 million worth in sales. The ADU was set up or is being pushed at the Urban Land Institute level [inaudible]. Being pushed is the solution for the housing shortage, but it sounds like it's more of a luxury item.

Bob: Yeah. Exactly. Upper middle income and upper markets is what I would target with it. We're looking at the territories in our area, and the ones we've mapped out, the 10 territories that in all likelihood we're going forward with, they're solid income areas.

Dan: Yeah. Now you're not constrained. Like me and the rental guys who are on the podcast listening right now are like, ah, how do we get the cash flow to match the 9% interest rate and blah, blah, blah, blah, blah. But instead, you have me being the successful business owner who's like, yeah, someday my aging parent or my college age kid coming back home, it's like, go out in the backyard, you got your own house [crosstalk] get out in the house.

Bob: Right, right. Take the dog with you.

Dan: That's cool. So it's been interesting and I guess the last friend that I've heard, or had a very limited experience, but maybe it was an Orange Theory guy that I was reading, but I think it was like a friend of mine that's playing a fitness franchise, and it was for the whole state of Illinois, I believe, you may have more, and he is like, it's too late. You just can't get into a plan. If it's the greatest thing ever, I'm so happy. I own so many and what shopping center do you have? Because I want to build another one and I own the territory.

Bob: Right.

Dan: But his comment was, the only way that you're getting in is if you bought someone else's. But the issue is with that is the star franchisees in the Planet Fitness ecosystem, they're just, oh, Illinois for Sale Shore. I'll take that.

Bob: Got it.

Dan: Now you're getting this consolidation effect of the most successful brands. Is that kind of what you were thinking with the men's health thing? Someone's going to do that?

Bob: Yeah, yeah. The relationship with private equity and franchising, private equity is all over and they pay stupid multiples. One of the strategies is, we ended up doing six. We would've ended up doing more once we got into it, but everything sold out too quickly. We have our six territories in New Jersey. We started talking about all territories, and as soon as we did sorry, that one that's gone, that's gone. Somebody came in and bought the rights to Chicago with that brand, 50 units. Two different people came into New York, 132 units, 134 units. Somebody else in New Jersey that's just to the northwest of us bought, I think they were five initially, but now they're up to, I think 18 or 19 units that they bought very quickly after that. Again, because it's just a strong economic model. This ADU concept that I'm mentioning, I'm starting to see a similar growth pattern, the activity around this brand. The men's health concept was probably the fastest selling brand I've seen in the last five or 10 years. This one may match, doesn't have the same level of sexiness as the brick and mortar men's health concept, but the ROI is better just because of scalability with this, how inexpensively you can get into it.

Dan: Why don't we talk just a little bit here kind of the cash to get involved, right? People are probably listening and like, wow, this is phenomenal. I don't have $1.9 million. What's the barrier to entry? If someone's listening right now, how much cash, how much net worth, how much experience? What's it take to actually be considered for a franchise?

Bob: Yeah. Well, it depends upon the franchise. The men's health concept, it was a half-million-dollar net worth and 100K liquidity that they were looking for. That was the minimum but they ended up not doing... They may have had a handful of single unit purchasers. Everybody was buying multiple units with that concept. The ADU concept as an example, it's a quarter-million-dollar net worth, it's low. Now, is that who's going to buy it? Not for the most part, no, because it's going to get bought up by larger players. But if somebody comes into this and says, hey, I have a liquidity of a couple $100,000 I'm willing to put into this. I have a million dollar plus net worth. You can buy five territories and you could do a lot of damage financially with five territories.

Dan: I guess it's situationally dependent, but if I'm the guy with two, 300 grands in cash and million dollars plus net worth, I'm like, Bob, let's do this. This is my plan, Bob. I want to get somewhere between three and 10 locations. We need to map out the plan. Maybe I have access to an investor pool and I can put together a million or two in cash from the people in my network already. Is this like I want to be in that five to 10 year and then flip out of it kind of thing and be done? Or is it better to kind of hold them for long term? Maybe with the men's health concept as the example, is there almost like a short fuse, right? It's so red hot that there's bound to be like the fitness example where there's a proliferation of other competing brands that maybe start to eat away the economics. So is there kind of like, look, we got to be out in three years and if we're not hitting our target, maybe we're actually modifying that. Talk me through sort of that timeline of hold from day one, if you would.

Bob: I would always look at an earlier exit strategy. If you get the number you want. If you have fantastic cash flow and it makes no sense to exit because you're just not getting the offer, stay in. To your point, what's going to threaten it? With the men's health concept, they do TRT, testosterone replacement therapy, ED treatments, weight loss with Ozempic and they do peptides. Okay. They're in some of the hottest things going, they're driven now, right now. The other profit centers are growing right now. It's like 70% driven by the testosterone, and that's membership base, typically 200 to $250 per month. Then you build a customer base and then you, and preferably, and that even works in blue collar areas, paycheck to paycheck. Guys, once they get on it never come at off. The other products are more expensive.

So, if you can get into an upper middle-income area with those types of products, you can do really well. I don't know what the legs on this are going to be. I know testosterone has been around for a long, long time. The data on it is getting better and better and it's very safe. So, I think that's going to have legs for a long, long time. Some of the other peripheral profit centers may change over time, but you have your core customer base, so I think it's going to have legs. The A DU concept, intuition just tells me that's long term. But would I sell if I have the opportunity to sell in a year, two years, three years at a strong multiple, I'm selling.

Dan: Yeah, yeah. Yeah. It's funny because that's what we have in the real estate community. We have fix and flip people. I love selling everything. I'm buying, I'm fixing, I'm selling. Everything's pretty much sale. Although I have this rental portfolio of apartments that I have the mindset of hold it forever. There're some guys at the extreme end, Bob guys, ladies, et cetera. There're investors on the extreme end, who like, I'm never selling anything. We could put our finger on the 88-year-old guy I talked to yesterday who's got about $20 million in industrial buildings, but he's actually talking to us to sell. So, I guess he's not the greatest example, but he did hold for 40, 50, 60 years, all these [indiscernible]. Right? So what percentage of the people who you've actually closed franchise with, I don't know, in a five, 10-year period, maybe it's 20, I don't know, whatever the length of time, what percentage of them are happy they've found something with cash flow and the hangs are 1, 2, 3 locations and you're just going to ride them forever. Versus the mentality that you and I kind of touched on today, where it's like, dude, everything's for sale. We're kind of looking at this like big capital flips. What percentage would you say are each?

Bob: It would depend upon the category of franchisee. If it's a franchise investor, which may be at any given year 10 to 20% of my client base, they're usually looking to flip.

Dan: Okay,

Bob: Three years, five years, and they're out. Maximize what your profitability can be and then flip at that point. Most others, 95% of those getting into it, they don't have that mentality. They want to stay in it. If they get in the right concept and they have really strong cash flow and they're spending less and less time with their involvement in the business, it makes sense to sit on it. I only recommend to my clients if it's a category that is, there's a threat to it in some capacity, like the video industry, then I'll gently say, hey, you might want to think about starting to put it on the market.

Dan: When you place someone in the franchise business, do you have a role that's capable? And if you're seeing that threat, you're calling those clients and saying, hey, I mean, is that something that someone could expect from you, Bob, if [crosstalk]

Bob: Absolutely. Yeah.

Dan: Okay. I guess it would too dictate which concepts an individual was going to be suggested they go to based on whether or not they're that 10 to 20%, like investor, flipper people, versus I'm just trying to quit my $85,000 a year job. I hate my boss and I've got my 400K sitting in an IRA and this sounds fantastic, and I can't wait to make 150 or 180,000 doing X, Y, Z. Like, you would know where to guide them in the industry.

Bob: Correct.

Dan: Yeah. Yeah. I feel like one of the big mistakes, and maybe I'm totally off base, but I feel like one of the big mistakes with franchises is someone sits down and like, what are the best franchises, they Google it and they like see oh my God, it's a McDonald's or whatever it is, and that's the extent of how they select.

Bob: I get questions all the time about like Chick-fil-A.

Dan: Okay.

Bob: Chick-fil-A is not even a franchise.

Dan: No, it's not yet.

Bob: It is a you're an indentured servant, okay? You're going to work for them. You're going to put 50 hours a week in and you make good money. You might make a quarter million, $300,000 a year, you're going to work your butt off and you don't own anything. You have nothing to sell. They own the building, they own the land. That's their gig. What's your question?

Dan: Yeah, it's the mistake that people make when choosing, because they probably have that affinity for Chick-fil-A, right? It's like, oh, I eat there. They look like they have lines all the time. They're a famous, popular company. I want to own part of that. Maybe there's some motivation where that is the right fit for an individual to say, dude, I want to spend 50 hours a week serving chicken. I don't care.

Bob: Yeah.

Dan: Quarter a million [crosstalk]

Bob: It could be

Dan: Fine. I don't care.

Bob: Yeah. Well, you, you see a lot of people. A large percentage of the population when I first start talking to them that aren't franchise investors, they equate franchising with food. The last thing I want to put anybody into is a food franchise. It is gotten dramatically worse over the last three, four years since COVID. You're managing you're managing food costs, you're managing labor, you're managing rent. Those margins have been ridiculously squeezed.

Dan: Yeah.

Bob: I never recommend food concepts. There're so many other things you can do too. People, when they start a franchise search, typically the average person, they're going online, they're googling when they do, your landing on portals. Maybe about 50 to 70% of the franchise companies out there advertise, pay to advertise on the portals, but 95% of the people coming to them through those portals end up not being qualified. So, they waste a lot of time, but you can't see what's behind a curtain because they're just showing you what they want you to see when you're going online and searching. That's why the companies would rather work with someone like me and look, I'm an independent consultant. I can go to any of the 4,000 plus companies out there. Do I do that? No freaking way. I try to stick to companies that I'm comfortable with maybe the top 10 to 20% in any given category of franchising. But then over the years, I've developed, which is an ever-changing list. I have about 75 brands on my list, and my focus is ROI earnings, don't give a what the widget is, as long as it's ethical, provides valued service to the community and 90% of those brands are semi-passive or passive brands because that's what most of my clients are looking for. That list is ever changing because like the men's health concept that I mentioned to you, it's off my list. As strong as it is, it's off my list.

Dan: Yeah.

Bob: Can't buy it. It's gone. There's no good territory left anymore.

Dan: I think I heard about that about a year-and-a-half ago. One of my buddies bought a few of them, two or three, and he knew the founder. I don't know if it's the same concept or not. It could just be a competing one.

Bob: Yeah.

Dan: I was like, man, that does sound great. I don't have the time to do it. I'm running this pretty substantial business already. I hear you saying like, ah, man, I would've loved to have had you to call and say, you, Bob, check this out. I got this buddy and he's telling me about this franchise. And if it was the right thing maybe it was you and I putting together the 6, 9, 12, 18, a few years. But I didn't have any expertise to go rely on. I appreciate your perspective flipping out of successfully the video trend in time, and then having this investor's mindset of franchise. Because before today's show, it's like, ah, dude, franchise chain yourself to the Chick-fil-A and never get to look up again. That was kind of how I thought of it and probably how people listen to the show is like, no, I'm not going to go install gutters for the gutter franchise thing and be the guy, but to be the investor who's buying and selling businesses as an asset, wow, that's attractive.

Bob: You know what? You mentioned gutters. I probably two years ago placed that year more people into a gutter concept than any other concept. Okay. I'll name it, the brothers that just do gutters, great company, they do have a semi-passive model. You might be 20, 25 hours in the early stages, but then you can really start to back off very scalable. My clients have done exceptionally well in that concept.

Dan: Nice.

Bob: There's money and gutters, man.

Dan: That's cool. Yeah, and I know because I want them for my house that I'm in right now, but I digress. Bob, as we switch gears for the wrap up here, do you have any book recommendations? We've got a real estate community, they're business minded, they're interested in ROI, maybe you have something in the franchise world that could help wet the whistle or just other really impactful books that maybe made a difference [crosstalk] in your mind?

Bob: Yeah, I love the E-Myth or E-Myth Revisited.

Dan: Nice.

Bob: It addresses franchising, but it really speaks to following a passion versus looking at a business logically. I always ask my clients upfront because I'm trying to ascertain exactly where they fall on the scale of people that I work with. For lack of a better term, on one end of the scale, I have what I term as ideologues. People who are passionate about something, they love their dog, so they want to be a pet related business. They love baking cookies, they want to be at a baking related business. On the other end of the spectrum, I have what you call my show me the money clients. Many of them are the franchise investors, ROI earnings don't give a damn which it is. Okay, as long as it's ethical, provides value service to the community, and can I do this on a passive or semi-passive basis? Where do you fall Mr. Client on that scale? That helps me determine the direction I'm going to take them in. Always trying to talk them out of the passion play, because you can learn to hate your passion if you're not successful financially with your passion, but you can learn to love something you're not in tune with if you make a bunch of money doing it.

Dan: That's right.

Bob: That's my philosophy anyway.

Dan: That's right, that's right. Crown jewel of wisdom, Bob, if you could go back to, I don't know, 1986, 1987, knowing everything you know about franchises in the business world now, what would be the crown jewel of wisdom you would share with yourself?

Bob: That's a great question. I would say that I would seek out someone as a mentor. People in my industry really didn't exist back then, but I just got lucky. I picked an industry that was a pretty hot industry, although it was probably already over the hump and started going the other direction. Fortunately, I did well with it. If I got in a little bit later it, could have been an absolute disaster. But I was just throwing darts. I was 27 years old, I had no idea what I was doing. I got lucky on my first one.

Dan: Nice.

Bob: Yeah, I'd seek out someone who's a mentor, who understands business, preferably someone who owns a bunch of franchises or has owned franchises maybe, or has been at a corporate level in one of the franchise company as a c-suite level, and ask their advice or seek out a good consultant that knows what they're doing. The issue with this industry, and I wish, not to disparage my own industry. I wish there would be regulation because so many people have come into this industry and these groups have developed where they'll charge people anywhere from like 20,000 up to $100,000 to get into one of these groups. They give them a couple of weeks of training a certificate and say, now you're an expert in franchising. They wash out in a year, but unfortunately, they hurt people. Make sure whoever you're going to work with has a background in franchising.

Dan: Very cool. Where can people get some more information? I guess, I thought you had like a guide to the [crosstalk] Yeah.

Bob: Yeah. I offer a free eBook on semi-passive franchising, is the topic of that. Yeah, anybody can go to my website franchisewithbob.com or you could email me at bob@franchisewithbob.com. Be happy to schedule a 30-minute call and see if it makes sense for us to work together.

Dan: Bob, my final question, what is the kindest thing anyone has ever done for you?

Bob: Man, that's a tough one. I don't know if this is the kindest, but it's one of the kindest things. Somebody invited me, offered me their vacation home to go and spend a couple of weeks there because I helped them get into a franchise and they had so much success with the franchise, so they were trying to repay me.

Dan: Nice. Very cool. Bob, I got a couple pages of notes. I had a blast with the conversation with doing my research. It's a totally different angle of the franchise approach, so I really appreciate you reaching out and taking your time to get on the show.

Bob: Thank you, Dan. It was fantastic, man. Anytime. Love to come back.

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