Public-policy skirmishes

Now two years after the COVID-19 outbreak, people are finally feeling like the pandemic has receded. Even Dr. Anthony Fauci, chief medical officer to President Biden, has announced the country is "out of the pandemic phase" and it is time for individual Americans, not government agencies, to assess their own COVID-19 risks.

For quick-service operators, this has meant an end to mask mandates (mostly), vaccine passes (mostly), occupancy limits and other public-health measures that were designed originally to combat the novel coronavirus and its variants.

But even as the masks have come down, battles over public-policy and public-health continue to erupt. Philadelphia's back-and-forth policy over mask mandates in April created confusion and consternation for businesses and people in the City of Brotherly Love. The Associated Press called it "a sense of whiplash" when the city reinstated its indoor mask mandate, a little more than a month after lifting it. City officials cited an increase in local coronavirus cases, but critics noted the action came when virtually every major city had removed similar indoor mask rules.

It is also worth noting that Philadelphia is among a handful of places that is extending benefits to workers impacted by the pandemic. The city's new Public Health Emergency Leave law guarantees up to 40 hours of paid, COVID-19 sick leave for eligible workers in businesses with at least 25 employees.

If there is one certainty, it is that business owners have to remain flexible in the face of changing economic and political realities. In many ways, the pandemic's grip over society has loosened, but its presence still hangs in the air and continues to fog things up. One reason Dunkin' has fared well in a challenging time is the laser focus of its operators. Great coffee and great service will always tip the scales toward the franchisees. Keeping an eye on the storm clouds outside is a good idea as well.

By Wendy Jacobson

Rising Rates, RISING RISKS?

What a time to be in business. As the pandemic recedes and we emerge from the past two years of COVID, many are looking for silver linings in the economic cloud. The job market is robust, the unemployment rate has fallen close to pre-pandemic levels at 3.6 percent, wages are rising and consumer spending is high.

At the same time, pent-up demand on items ranging from cars to restaurant meals (along with the workers to provide them) has sped past the supply levels, leading to record inflation and rising costs for virtually everything. The Federal Reserve has stepped in with incremental hikes in interest rates to try to slow things down, which has made borrowing money more costly as well.

Some say the Fed's rate hike will cause a recession, while others aren't so sure. Regardless, quick-service operators and other business owners are dealing with a variety of issues making it anything but business as usual.

A BUMPY ROAD

While many restaurants shuttered during the pandemic, unable to survive the various bumps in the road, Dunkin' emerged strong.

"Dunkin' franchisees are some of the most resilient people I've ever worked with," says Tom Fitzgerald, director of Franchise Finance at Bank RI. "They've tackled COVID and labor shortages over the past two years, and now inflation and the rising cost of borrowing. It's a lot but I'm confident they can handle it."

Fitzgerald believes that even with interest rates rising, we're not going to see inflation recede right away, which means franchisees who are embarking on remodels or new store construction need to manage their risk appropriately.

"There are a few ways they can structure a loan as floating rates continue to rise – especially for extending construction periods – such as borrowing the entire amount at the start of construction and placing the funds into escrow [to eliminate] rate volatility. It's critical now more than ever to work with a financial partner who can provide flexibility and several options," Fitzgerald says.

In addition, he recommends franchisees pay close attention to their overall fiscal management right now. "A strong balance sheet and liquidity means franchisees may not have to borrow as much, and ensures they have the means to support any downturns in the future."

Lindy Baldwin, managing director of Franchise Finance at Webster Bank, agrees. She says higher interest rates on loan payments equates to less profitability, which can cause the franchisee to tap the brakes on any needed financing. If that's the case, they may have a couple of other options.

"Some franchisees are sitting on a lot of cash due to the Paycheck Protection Program (PPP) and Economic Injury Disaster Loans (EIDL) from the pandemic. If this is the case, they can dip into their balance sheet to fund the necessary

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projects should they not be comfortable with the rates," she told Independent Joe in an email exchange. "They also could potentially invest any excess cash into interest bearing accounts to profit more money because during times with high interest rates, businesses can earn more money from investments."

TOO HOT TO HANDLE?

Rob Branca, whose company, Branded Management Group, owns 60 Dunkin' stores in two states and recently sold 31 Ohio Dunkin' shops to Inspire Brands, says he is not concerned about the current confluence of factors making the money supply tight.

"Even in this environment, Dunkin' will fare well because we have the tools to do so. For example, we are uniquely positioned to navigate supply chain issues with the National DCP, and with the right balancing act, we can successfully navigate through inflation and rising rates," says Branca. "Of course, we need our guests to be resilient as well. If they stop coming in, nothing else matters."

Recognizing that franchisees still need to remodel current stores and construct new ones, Branca stresses the importance of franchisees getting the best ROI on their investment, now more than ever. "That means ensuring the end product is a beautiful place where people want to be, both employees and customers," he says. "It's particularly important to create a good environment for the crew so they want to work because turnover is very expensive,"

For franchisees who are remodeling, he suggests increasing operational efficiencies, such as maximizing throughput in the drive-thru; optimizing the layout to get more done with less crew members; and decreasing the number of steps crew members need to take to complete a task. In terms of building new stores, Branca says focus on getting the best possible location. "We've been spoiled by cheap money for a long time, and even though rates are rising, they are still low," he said. "Premium locations may come at a premium price."

WORK THROUGH ANY FATIGUE

Even with rates still relatively low, business owners have not been operating in a rising rate environment in a long time, which might cause some stress or anxiety. "I imagine many franchisees are experiencing fatigue given everything they've had to endure over the last two years, from a shortage of employees to the rising cost of goods and inflation. Ensuring they are surrounded by a strong team of partners who can help them navigate the waters and chart the best path forward in good times and through downturns," Bank RI's Fitzgerald says.

Franchisees might experience sticker shock when getting quoted term sheets because rates have not been on the increase for many years, adds Baldwin of Webster Bank. "For example, franchisees looking to expand through acquisition need to ensure the deal makes complete sense before moving forward," she says. "Paying a premium for an acquisition now comes with the hurdle of a higher rate, which is something borrowers haven't been accustomed to in a very long time. Healthy cash flow can help buffer those higher rates on loan payments should the franchisee want to acquire."

In addition, franchisees need to be prepared for what might be coming down the pike. "I like to counsel my clients to run different analyses to see the impact of rates going from, say 5 percent to 7 percent," Fitzgerald says. "It's important to be aware of rate sensitivity and so that you are prepared for volatility, if it should come to that."

No one has a crystal ball to determine when the current environment might ebb. That means franchisees need to be proactive and meet regularly with their financial team to get in front of things.

"That way, they can focus on what they need to, which is running their business," says Fitzgerald.

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