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How to Finance Your Franchise Investment

(Psst, it's easier than you think!)

So, you are thinking about investing in a franchise. First, good choice. Franchising offers you a great path into business ownership with a proven model, organized support system and a team to help you every step of the way.

As you move through your decision process, one of the big questions that you will need to answer is how you will finance your investment. Use your own cash? Bring in a partner? Take out a small business loan? Utilize retirement funds through a qualified rollover?

In short, you have TONS of options. Here is a brief overview of financing options to help you evaluate your choices.

Big Picture - Compare a franchise investment to buying a house

At a very basic level, most franchise investors will choose to combine equity and debt to acquire their franchise, similar to when you acquire a house. With a franchise investment, you should expect to contribute 30% of the total project investment in some form of equity (we will survey the options in just one minute). You can typically borrow the remaining 70% through a small business loan.

There are 3 major sources of your equity down payment

Each potential franchise owner has a unique financial profile. Consequently, each person's sources of capital will be individual. There is not a universal right or wrong. It is simply a personal preference.

The most common source of equity capital is for a candidate to use personal, non retirement account savings. This is money that you have been accumulating in your "rainy day" or "special investment" savings account. This is money that you have set aside for a special investment but you just did not know what it was or when it would present itself. This is most commonly used because it is readily accessible, low cost to access and allows you to maintain 100% control of the investment.

A second commonly used source of equity capital is to utilize a retirement account rollover. Tens of millions of us have been diligently saving into IRA and 401-k accounts throughout our careers. We have set that money aside for long-term investment so that we can enjoy a more financially comfortable retirement. But, in a traditional plan, we have no ability to access or leverage that capital today.

With a retirement account rollover, you have directly invest that money into your new business instead of a portfolio of stocks, bonds and funds. With a qualified retirement account rollover, you are not subject to taxes, penalties, interest or any problems. Instead, you are able to utilize your retirement account funds to make a long-term investment in yourself!

The third major source of equity capital is to partner with an investor who has cash to invest but wants to leverage your talents to operate the business. These partnerships can be extremely successful if both partners can into the partnership with a clear vision of the goals and financial structure determined. Bringing a partner into your investment can enable you to build a larger business faster as well!

Loans are plentiful for franchise investments

One of the best elements of franchise investing is that loans are readily available to invest in franchise businesses. Though your new franchise business is technically a start up company, banks are willing to lend money to your franchise business because they are able to see the track record of success that the brand has enjoyed in the past in other locations.

Within the franchise world, the vast majority of business loans will be structured as "SBA Loans". Here is what that means – your bank will make you a business loan on terms that you negotiate with them. As additional repayment protection, the bank will ask the US government to "guarantee" repayment of a certain percentage of the loan. In this case, the "guarantor" will be the Small Business Administration. In exchange of this guarantee, there is a slight interest rate premium on the loan and a guarantee fee which is a one time closing cost to the loan.

The SBA loans are a great option to have. You should also consider other lending options that are typically faster and less expensive. If you have accumulated significant home equity in your real estate, you can leverage that equity and setup a home equity line of credit to borrow against your own equity. Similarly, you can setup a margin account with your investment house to borrow against the equity in your non-retirement investment account. Both of these are great options which have less red tape and lower overall costs.

Bottom line – You have options

Regardless of the size of the investment or the industry in which you want to invest, you have a multitude of financing options within the franchise world.

If you want to discuss franchise options or franchise financing in more detail, visit Chris Cynkar at 412-877-2000, ccynkar@franchoice.com or www.chriscynkar.com.