[EBOOK]

The franchise territory design guide









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Dustin's professional trajectory encompasses a range of roles, from combat veteran to successful service business owner and entrepreneur. Notably, he contributed to the growth of home service brands during his tenure as a Franchise Development Director at BELFOR Franchise Group. As CEO of Insulation Commandos, he leverages his diverse background to lead the franchise with strategic vision and operational excellence.

Introduction

How you set up franchise territories can either make or break your franchise game. If the territories are too sweet for the franchisees, your business might miss out on some serious growth. But if they're not appealing enough, good luck finding anyone to join the franchise party!

Designing territories is part of the franchisor's know-how, and as such, it is at the heart of your franchise model.

No one-size-fits-all rules here because every business has its own quirks, limits, and vibes. Still, there are a few basic principles you can roll with to figure out how to design your territories.

So, here's the guide to discovering your secret sauce that'll spice up your repeatable success recipe!

1. Understanding Territories

Before getting to the heart of the matter, here are some definitions and reminders to be clear about what we are talking about when we talk about territories.

1.1 Franchise territories

A franchise territory refers to a specific geographic area or region within which a franchisee is granted the exclusive or semi-exclusive right to operate a franchise business. The purpose of establishing franchise territories is to ensure that franchisees have a defined market in which to operate and build their business without direct competition from other franchisees of the same brand within that territory. This can help protect the interests of both the franchisor and franchisee. The scope, size, and level of protection within the franchise territory have to be described in the FDD (Franchise Disclosure Document).

There are generally two different types of franchise territories:



Exclusive territories

An exclusive territory ensures that the franchisor will not grant new franchises in the area, and is not allowed to sell to clients in the area, whether via physical premises or online.



Protected territories

They usually refer to various degrees of protection. For instance, the agreement may prevent the franchisor setting up other franchises in your neighborhood, but it might allow the franchisor to target online customers in your area.



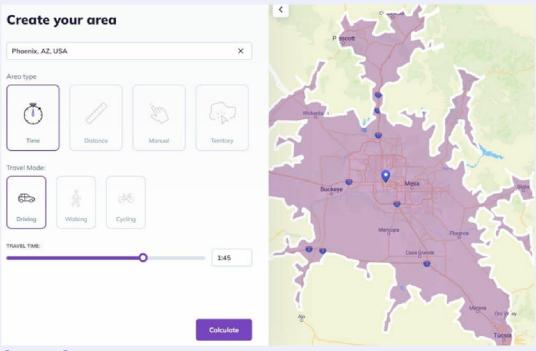
Dr. Tom DuFore:

"I often emphasize the strategic importance of what I like to call 'marketing territories,' where franchisees are responsible for their own marketing. In service-based franchises, it's not just about securing an exclusive area; it's about maximizing the local market potential within that space. By focusing on a marketing territory, franchisees can enhance their profitability and effectiveness, ensuring they are not spread too thin. While having a protected territory has its merits, the key lies in striking a balance between local focus and the flexibility to capitalize on opportunities, even those slightly beyond the borders of their designated territory."

1.2 Catchment areas or trade areas

The catchment area, or trade area, determines the addressable area for a franchisee. This term is mainly used for fixed location businesses. It refers to the area where the customers are coming from. For instance, the trade area for a restaurant in a suburban area may be around 10 minutes drive time: that's where above 80% of your customers are coming from.

Catchment areas are helpful to understand customer behavior, and are a good start to estimate the potential for a new fixed location.



Source: Smappen

1.3 Service areas

Service areas are relevant to mobile businesses. It comes down to the area where the franchisee will be able to service its customers. For instance, a home care service franchise will choose to provide its service within a 10 driven miles radius from its locations, to avoid high operating costs related to travel time and costs.

Service areas are defined by the franchisor, and often correlate with franchise territories when exclusivity is granted.



2. Why you should define franchise territories

Although most of them do, not all franchisors award franchise territories. But making use of them provides some advantages.

2.1 Secure candidates

Franchise territories help franchisees by providing a degree of exclusivity, market focus, and local knowledge that can enhance their chances of success and profitability within their designated areas.

As franchisees typically make a significant financial investment to join a franchise system, having an exclusive or protected territory provides a level of security.

It reduces the risk that a new franchisee will open in close proximity and undermine the original franchisee's investment, and is an important factor in their franchise choice.

2.2 Ensure optimal coverage

If you're not maximizing your territory coverage, you're leaving money on the table. Coverage directly impacts your revenue, as it influences your market penetration and your brand recognition.

Designing franchise territories helps optimize and maximize the coverage, and avoid white spaces that are not covered by your franchise. White spaces can account for up to a 60% loss in potential for a franchisor!

You should aim at avoiding unserved customers, even though you won't necessarily be able to ensure 100% coverage—some territories just don't have enough potential to justify investing in a new location.

2.3 Avoid cannibalization

Cannibalization results from overlapping catchment areas, often due to poorly sized or neighboring zones or the addition of a new store in an area served by an existing franchisee. This proximity immediately leads to under performance in sales for affected locations.

Defining territories in a way that avoids catchment areas or service areas overlap ensures that you won't have any cannibalization issues.



2.4 Prevent conflicts

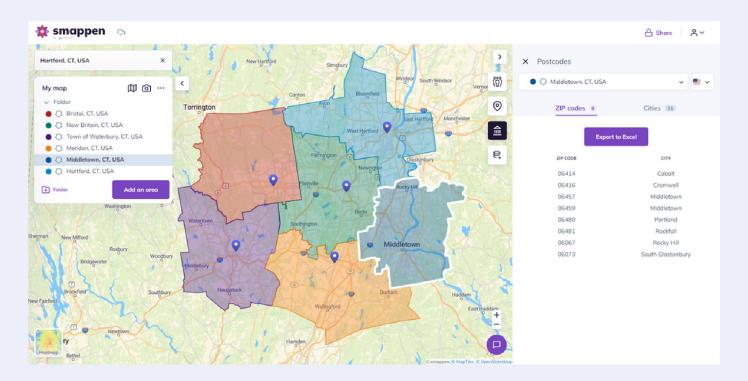
Without clearly defined franchise territories, franchisees' areas of operation are not wellestablished and can be a breeding ground for disputes. This can lead to disparities in terms of potential for success or territory size. ultimately resulting in revenue imbalances and conflicts between franchisees, and in some cases, between the franchisor and franchisee.



2.5 Assign leads and online sales

If you generate leads or online sales and want to allocate them to your franchisees, you'll need to define who gets what. Territories are a good way to handle this, as they will also allow you to optimize the costs of delivering your products or services by assigning them to the closest franchisee.

Franchise territories can be used as a reference to assign these new business opportunities to your franchisees: any new opportunity in the territory belongs to the respective franchisee.





Dr. Tom DuFore:

"I've observed that undefined territories can lead to significant challenges.

Firstly, without clear boundaries, franchisees may engage in counterproductive competition, turning what should be a cooperative network into a free-for-all. It's vital to assign specific territories to each franchisee, giving them a sense of ownership and responsibility. Secondly, if franchisors don't proactively define these territories, franchisees will inevitably do so, often in ways that may not align with long-term strategic goals. This lack of clarity can later hinder market saturation efforts, devalue the business during investment rounds, or complicate acquisition processes."

3. When you should define franchise territories

Territories can be designed at different stages of your franchise sales process. Knowing when the best time is will depend upon the stage of growth your franchise is in.

3.1 In an opportunistic manner

Emerging franchisors usually begin by defining their franchise territories opportunistically whenever new franchisee opportunities arise. This is a good starting point, especially as early-stage franchisors often lack a well-established track record, leading to an evolving definition of their territory design criteria. This approach allows room for learning and improvement. Typically, the initial territories assigned tend to be generously sized and filled with potential. Over time, as the franchisor gains experience and confidence, they can fine-tune the new territories to their optimal size.

However, this method has some drawbacks, including:

- Lack of a clear plan: Similar to a leaf carried by the wind, you expand according to opportunities, not knowing where you will land.
- Territory over-sizing, often driven by candidate demands, can be challenging to refuse.
 Over-sized territories represent untapped potential, meaning you might have one franchisee where there could be three or four. Many locations that could have been established will never see the light of day.
- Another risk of opportunistic development is the creation of white spaces. Dividing territories without a prior plan is akin to randomly tossing puzzle pieces and hoping they will fit together well.



Dustin Ingle:

"I prefer involving franchisees in finalizing their territories, as they have knowledge of the local area and market. Together, we can develop a territory that will enable the franchisee to maximize their revenue."



Dr. Tom DuFore:

"I believe that having at least a rough outline of a territory is going to be important right from the very beginning. Then, you can define that territory more precisely with each franchisee."

3.2 Upfront

Another approach is to plan a few steps ahead and define franchise territories proactively, even before you have candidates for these areas.

By doing this, you will adopt a different mindset: you will initiate a development strategy, assess, and prioritize your next steps.

This approach offers the following advantages:

- Logistics Optimization inventory management and delivery issues are often critical for franchise networks, especially in the retail sector. Prioritizing new locations to have multiple franchisees in a geographic area can streamline efforts, such as offering a centralized storage facility.
- Time Optimization: effective network management is crucial for the well-being of the network, and the efforts provided must meet expectations. This includes events, meetings, discussions, knowledge sharing, and ensuring the correct application of the concept. Your field consultants regularly visit franchisees. Regional management should help save time on travel.
- Cost Optimization: the final reason is, of course, a direct consequence of the previous two reasons. Optimizing logistics and time ultimately increases the profitability of your actions. Less time spent means optimizing your efforts and, therefore, your costs. Keep that in mind!

Applying this process to your entire potential market will enable you to go a step further: defining your development plan.



Dustin Ingle:

"In some cases, you need to plan ahead, especially in large cities. You don't want to carve out three territories for someone and then leave a small section that's too insignificant to be awarded as its own territory."



Dr. Tom DuFore:

"I don't recommend building out every single territory right from the beginning, especially in a vast country like the United States. However, as you start selling franchises in various metropolitan areas or cities, it's important to begin segmenting those areas. For instance, if you aim to sell in the state of Florida, particularly in Miami, having predetermined territories for Miami can be very helpful in the sales process. It allows you to show prospects what's available."

3.3 Building your development plan

The establishment of a development plan involves mapping the entire target country by determining territories for current and future locations and prioritizing them. This allows for the optimization of a brand's territorial coverage in a given area and ensures controlled growth.

This analysis serves the following purposes:

- Ensuring the repeatability and potential of the concept across the entire territory.
- Identifying future deployment areas and organizing the development strategy.

Furthermore, the development plan serves as a compelling selling point for potential franchise candidates. It demonstrates the seriousness of your strategy and the longevity of the brand. Creating your development plan is an essential step in expanding your network. There is no precise rule regarding when it should be carried out. It should be conducted early enough to prevent opportunistic development but also late enough to have sufficient data on your existing locations to define reliable criteria and conduct a thorough analysis.



Dr. Tom DuFore:

"Careful planning is crucial in the initial stages, particularly with the first 50 franchises. By thoughtfully defining territories from the outset, franchisors can avoid inadvertently restricting future expansion and franchise sales, maintaining both growth potential and market effectiveness."

4. How you should define your franchise territories

Territories are defined by their size, shape and potential. These elements are intricate and influence each other. Designing a territory is about finding the perfect balance between these three variables.

4.1 Choose your reference locations

To define these success criteria, you should model them on your existing locations. Select those that are successful and generate suitable revenue for your business, as well as those that are less successful—these also provide valuable insights. Be cautious to not only choose the overperforming locations, as they may not be representative of your entire network. It may not necessarily be the first outlets opened but rather those that best reflect your brand and positioning.

It is on this basis that you will start your study.

4.2 Know your typical influence area

The first element to know for the creation of your franchise territories is the typical influence area of your locations.

For fixed location businesses, it is necessary to know your typical catchment area. It will show you how far your customers are generally coming from. This is a great indication to define the maximum size for your territory: above this limit, your location won't be able to have a significant market penetration.

For mobile businesses, you'll look at your typical service area. This is important to take your operating costs into account: above a certain distance, it will become unprofitable to service customers.



4.2.1 Typical catchment area

If you're a fixed location business, your typical catchment area is generally defined as the drive time area within which are 80% of your customers. There are different possibilities to estimate it, depending on the available customer data that is available.



If you have customer location data

If you have customer databases with their addresses, you'll be able to precisely evaluate your typical catchment area.

Take some of your reference locations, and assess their catchment area: all you need to do is to plot your customers on a map, and draw a drive time area that contains 80% of your customers. This drive time is the location's catchment area.

For instance, if a 20 minutes drive time contains around 80% of a location's customers database, then 20mn drive time is the catchment area for this location.

Perform this analysis for some of your reference locations, and keep the average.



If you don't have customer location data

To overcome the lack of customer data, don't hesitate to conduct a survey at your points of sale to understand your customers' mobility. How much time do they spend traveling to reach your store? By what means (on foot, by car, using public transportation)?

You can use the results of this survey to define your typical catchment area.

4.2.2 Typical service area

If you're a mobile business, you need to define the maximum distance or drive time you want to service. It's a financial tradeoff, that is necessary to ensure minimal margins and profitability:

- Distances will generate operating costs, related to fuel, vehicle maintenance costs, ...
- Drive times generate costs as they're non productive and don't generate revenue.

It's also possible to adapt your pricing according to these costs, but you must keep competitiveness in mind when doing so.



4.3 Know your territory design criterias

The success criteria are the foundation of the franchise. They guarantee the replicability of the concept in the territory. These criteria are the indicators that allow evaluating the market potential in the area and sizing it accordingly. They are primarily related to your target audience.

4.3.1 Define your ICP

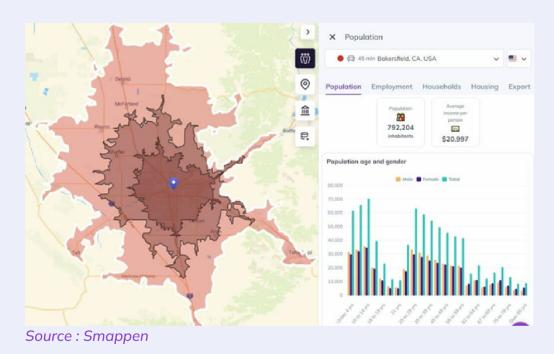
Defining your ideal customer profile will help you identify the metrics you have to look at to define your design criteria.

Your ICP should include the key characteristics of your main targeted customers in terms of demographics (for B2C) or business type (for B2B).

You can identify these characteristics using:

- Customer data: if you have enough detailed information, analyzing your customer database can help you identify recurring factors among your most valuable customers.
- Existing territories analysis: if you don't have detailed customer data, you can start by looking at the statistics within your existing territories, and identify recurring patterns.

Commonly used characteristics in B2C are: age, revenue, family size, education...



4.3.2 Quantify key success factors

Once you know your ICP and associated metrics, you need to quantify you key success factors. The objective here is to define what is the minimum value for your different metrics to ensure that a territory is viable.

- Look at successful locations: your successful locations will tell you which values are acceptable to define a viable territory. They set some references, but not necessarily the minimum values (a franchisee can be successful with an oversized territory).
- Look at unsuccessful locations: you can learn from your unsuccessful locations, if you have any. They will tell you which metrics values may put your locations in a danger zone.

An example of quantified key success factors could be:

- Minimum 50 000 people
- Median household income above \$60000



Dr. Tom DuFore:

"As for metrics, starting with the total population tends to be the easiest approach. To delve deeper, I generally advise looking at your customer base and using that as a key driver."

4.3.3 Other criteria

It can be interesting to look at some other factors that can have a substantial impact on your business, such as:

- Brands with similar targets: know who your best neighbors are, and locate them. They're the ones who have a similar ICP, and, ideally are renowned enough to attract a consistent flow of potential customers close to your future business.
- Prescriptors or referrers: if you have businesses that can recommend your products or services, it's a good thing to have them around.
- Competitors: this one is a double-edged word. Competitors can of course be a threat, but also a good indicator that an intereting market is there.



4.4 Pick the right geography

There's more than one way to map out <u>t</u>erritories, and it all boils down to how you want to measure things. Specifically, you can define your territories in one of four ways.

Distance radius

Definitely one of the simplest way to define territories, distance radiuses define territories as circles on a map. The biggest issue with this kind of approach is that circles don't fit well together. You'll either have:

- Blank spaces between your territories, leaving potential customers unserved
- Overlapping territories if you want to ensure a full coverage, opening the door to territory disputes.

Manually drawn area

You might be tempted to do things the old-fashioned way. You don't necessarily need to break out pen and paper to use this method, though, as you can use online mapping tools to do this. However, it will create ambiguous boundaries that can only be described with a map and leave room for potential unwanted debates.

Isochrone or isodistance area

When drawing an isochrone area, you pick a travel time (like half an hour) and a means of transportation (like driving) and use that to define your territory. An isodistance area is similar to an isochrone area in that it represents real-world conditions, only with distance instead of time.

The biggest advantage of this method is it gives you a territory that accurately communicates real-world conditions. That means it's closer to representing actual customer behavior or serviceable areas than some other methods.

It's not necessarily best suited to drafting a franchise agreement. You can't really define a territory as "an area covering a 15-minute drive in every direction from 872 Pine Hill Road." Franchisees will expect something a bit more concrete, and it's recommended to have a definition that leave no space to disputes.

Administrative boundaries

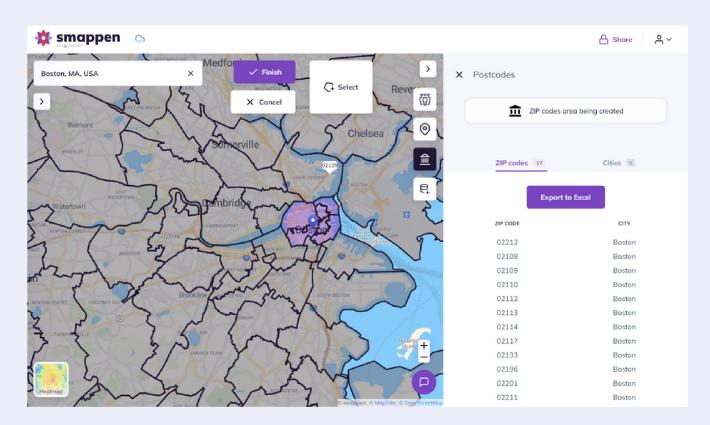
From a legal perspective, this may be one of the simplest ways to map out franchise territories, and that's one of this method's greatest advantage. Administrative boundaries are incredibly easy to communicate; you just have to list them in your contract. This leaves no room for conflicts between franchisees. Most franchisors use ZIP codes to define their territories, or Counties in some cases.

Above all, administrative boundaries are like a puzzle you can play with, define scenarios and iterate to draw your way to an optimal coverage of your targeted country. Clearly, we highly recommend this methodology to design your territories.



Dr. Tom DuFore:

"I like to use zip codes because they're easy to use and very clear. It makes it easy for marketing."





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4.5 Design your new territories

Using your selected geography, you can draw a first draft and iterate to find the optimal territory for a new franchisee.

Here are a few guidelines you can follow.

4.5.1 The minimum size

Each territory should offer enough potential for the franchise to succeed. If a territory is undersized, the franchisee is set up for a project doomed to failure.

That's when your quantified key success factors prove to be useful: the minimum size for a territory is the smallest territory you can draw that complies with your key success factors.



Dr. Tom DuFore:

"One of the mistakes I've observed is when a franchisor, starting as an emerging brand, initially sets territories that are too small. You really want your first franchisees to be successful. If you figure out the initial territories are too small, don't hesitate to go back and expand those territories to adjust accordingly."

4.5.2 The maximum size

It can be tempting to compensate for an undersized area by increasing its size. A larger territory may have greater potential, but it can also conceal additional costs or unintended impacts.

Your typical catchment area or typical service area will help you set the limits and avoid sizing a territory above its reachable market.

- For catchment areas (fixed location businesses): outside of your catchment area, chances are high that potential customers won't make the trip to your location. The franchisee will have a very low market penetration, wasting revenue potential.
- For service areas (mobile businesses): outside of your maximum serviceable area, the franchisee will either have high operating costs and decrease their profit margins, or won't service these areas at all, leaving potential customers unserved.





Dustin Ingle:

"In rural areas, you may reach your target number of people with spread-out territories. However, it could be a three-hour drive from one end to the other. For a new franchisee with a single truck, starting out with a drive time radius of one hour is the furthest they should go to avoid additional costs."



Dr. Tom DuFore:

"I would rather start with a territory that is too large. Erring on the side of larger territories has much less impact on your franchise than starting with territories that are too small, which could put your first franchisees at risk."

4.5.3 Common mistakes

There are a few common errors you should be mindful of while designing your territories:

Ignoring existing locations:

carefully consider your existing network to avoid any risks of cannibalization. Mapping your locations' customer databases can help you identify such risks.

Sacrificing future locations to close a deal:

sometimes, extending a territory will compromise the viability of a neighboring territory. Avoid closing a deal that may result in losing another.

Giving away market potential to close deals:

avoid doing favors for candidates without receiving something in return. At the very least, adapt your price to the territory's potential.

Seeking perfection:

you probably won't achieve 100% coverage of your target country, especially if you're a mobile business. Some areas are just not worth the investments and operational costs.

Not taking ground reality into account:

ensure that the territories you design align with terrain reality, local habits, or operational constraints. Consider natural barriers like rivers and make territories accessible and serviceable.

Not considering channel conflicts:

make sure you consider other existing channels such as selling products online, selling at other local retailers, and operating in unique venues (sports stadiums, universites, ...) when designing your territories.

Creating unbalanced territories:

aim to design balanced territories, providing all franchisees with a playground for a successful launch and development. Unbalanced territories can lead to disputes with franchisees who feel their deal was unfair compared to others.



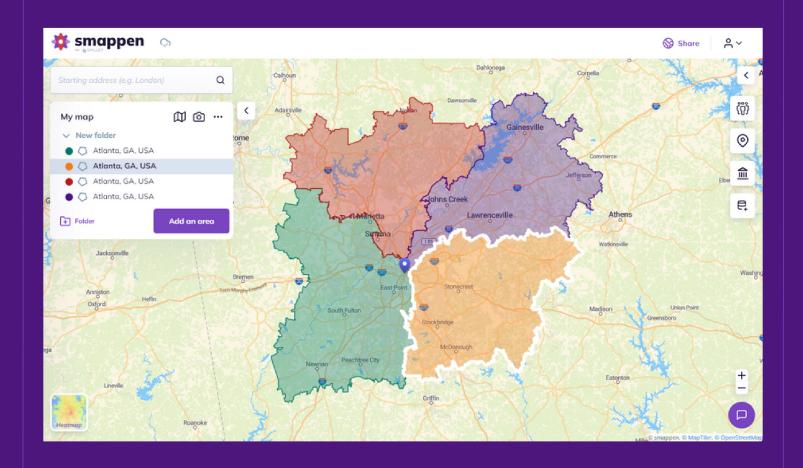
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Cutting a city into slices

In large cities, there is often the opportunity to establish multiple franchises. Ideally, we recommend awarding these territories to a multi-unit franchisee to avoid unnecessary splitting. However, it may be necessary to divide these cities into several territories.

It's a complex exercise. Indeed, each city is heterogeneous, with urban areas, outskirts, affluent neighborhoods, and popular neighborhoods, each with different characteristics. It's not easy to create equivalent zones under these conditions!

One possible strategy: dividing it like a cake. Here, the goal is to cut equivalent portions in terms of potential and characteristics. For example, a city can be sliced like a pie chart, so that each franchisee can have a part in the city center and a part in the suburban area. Don't aim for perfection, aim to be fair; that's already very good.



5. Exploring new and promising territories

At the beginning of your franchising adventure, it seems like there's potential everywhere, and it can be challenging to determine where you should start first.

Conducting a few analyses can help you quickly identify the most promising territories and focus on easily attainable opportunities.

5.1 Look at the distribution of success factors

Your key success factors are your best indicators to assess the potential of an area. So look for areas where these factors have the highest score.

Heatmaps are great to visualize success factors, such as:

- Median household income
- · Population density
- Median age...

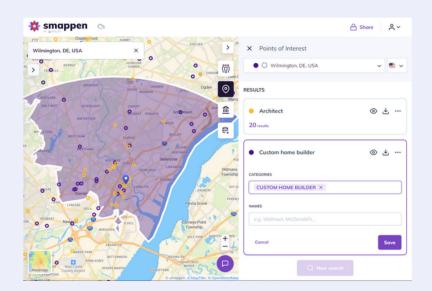


5.2 Spot competitors

If there's no competitor in the market, there's probably no market. The opposite is equally true: if there's a market, there should be competitors around.

Map your competitors to identify interesting areas, especially the well-performing competitors.

Chances are high that they've done their work and have seen potential in the areas where they're located. Identify the best competing brands and see where they are.

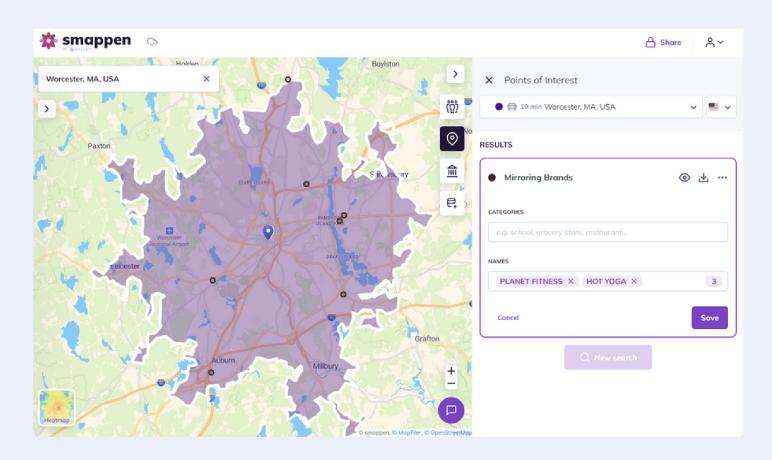


5.3 Locate mirroring brands

You probably know some brands that have a similar ICP but aren't direct competitors. They target the same profiles but offer different products or services than yours. The presence of these mirroring brands is a good indicator that there may be an interesting concentration of your ICP in the area.

If you can't think of a specific brand, it may also be businesses offering products or services that your ICP usually buys. For instance, if you're offering healthy food, locating fitness or yoga centers may be a good starting point.

Moreover, having them around will also generate some traffic that you can benefit from, so you should definitely take a closer look at areas where you have this kind of neighbors.



Conclusion

So, there you have it - your ultimate guide to the art and science of franchise territory design, that can make your franchising game a hit.

Now, as you gear up to explore new and promising territories, armed with insights on success factors, competitors, and mirroring brands, consider this guide your compass.

But remember, this is just the beginning of the adventure. The real fun begins when you start mapping out those territories, creating your franchise masterpiece. So, grab your map and let the franchising exploration begin!

Acknowledgments

Our sincere thanks to <u>Dr. Tom DuFore</u>, CEO of Big Sky Franchise Team, and <u>Dustin Ingle</u>, CEO of Insulation Commandos for their invaluable contributions to this ebook. Their expertise and insights have been instrumental in shaping the content and enhancing its quality. We are grateful for their meaningful collaboration.

To contact and learn more about Big Sky Franchise Team visit: bigskyfranchiseteam.com

More about Insulation Commandos franchise:

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