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FRANCHISE BUSINESS ECONOMIC OUTLOOK 2020

Franchise Growth Continues

Prepared for the
International Franchise Association

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Franchise Business Economic Outlook for 2020

- Franchise industry growth is expected to continue riding the momentum of the U.S. market boom in 2020, despite an uncertain economy.
- The number of franchised businesses in the U.S. is expected to grow by 1.5% this year, to a total of 785,316 establishments.
- Franchise industry expected to add 232,000 jobs in 2020, growing total employees to 8.67 million.
- Franchise businesses' economic output is expected to grow faster than the economy as a whole.
- Overall GDP contribution by the franchise industry is expected to grow by 4.6%, to $494.96 billion.
- The industries with the most expected growth are projected as: personal services, quick-service restaurants (QSR) and full-service restaurants.
- The states that will see the most franchise establishments and employment growth in 2020 ranked in order are: Texas, Colorado, Arkansas, Florida, Idaho, Tennessee, Georgia, North Carolina, South Carolina, and Nevada.

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Executive Summary

Franchise industry growth **expected to be strong**, despite an uncertain economy

The number of franchised businesses in the U.S. expected to grow by **1.5%** to **785,316 units**

The number of people employed by franchised businesses to grow to **8.67 million**

The franchise industry is responsible for creating tens of thousands of opportunities for small business ownership and millions of jobs for employees across America. Its locally-owned franchises are America's hidden small businesses, with 773,600 small franchise establishments across the country. In 2019 alone, these establishments supported nearly 8.4 million direct jobs, $787.5 billion of economic output for the U.S. economy and represented 3 percent of the total Gross Domestic Product (GDP).

Locally owned franchises are America's hidden small businesses, with 773,600 franchise establishments across the country.

In order to assess the strength of these industries, the International Franchise Association (IFA) engaged with FRANdata to prepare an Economic Outlook Report. The report includes an overview of the franchising industry's growth trend from 2016 to 2019 and forecasts the industry's performance for 2020, and also includes a state outlook for all 50 states and Washington D.C.

The franchising industry continues to pride itself on its positive impacts on communities across America and looks to further identify opportunities for continued growth each year.

GDP contribution by the franchise industry expected to grow by **4.6%** to **$494.96 billion**

The industries with the most expected growth will be personal services, quick-service restaurants (QSR) and full-service restaurants

The states that will see the most franchise establishments and employment growth in 2020 ranked in order are: **Texas, Colorado, Arkansas, Florida, Idaho, Tennessee, Georgia, North Carolina, South Carolina, and Nevada.**

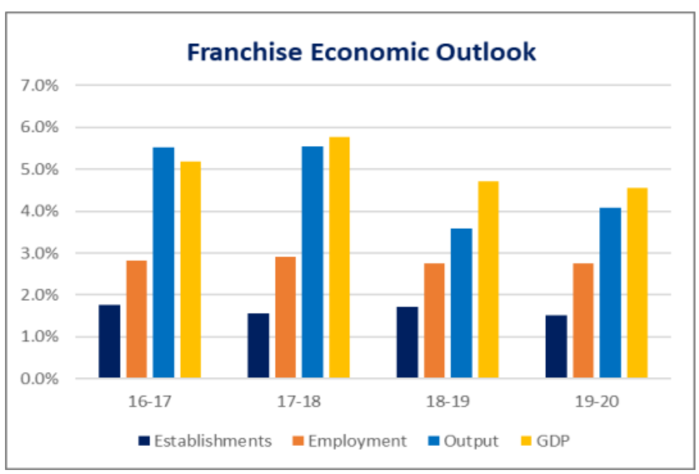
The U.S. economy grew at a moderate 2.1% in the third quarter of 2019[1]. Our analysis shows that, in 2020, increasing consumer spending, rising disposable income and a strong labor market will enable the franchise industry to experience another year of strong momentum in 2020 and continue its significant impact on the U.S. economy.

In 2020, the number of franchise establishments is expected to increase by 1.5% to 785,316. Franchise employment is forecast to increase by 2.8% to 8.67 million, adding a total of 232 thousand jobs. Franchise output in nominal dollars is projected to improve by 4.1% to $819.57 billion in 2020.

Franchise Business Economic Outlook: 2016-2020

	2016	2017	2018	2019 (Est.)	2020 (Proj.)
Establishments	735,847	748,752	760,476	773,603	785,316
Percentage Change		1.8%	1.6%	1.7%	1.5%
Employment	7,756,202	7,975,179	8,207,599	8,434,090	8,666,141
Percentage Change		2.8%	2.9%	2.8%	2.8%
Output ($billion)	$682.75	$720.44	$760.31	$787.51	$819.57
Percentage Change		5.5%	5.5%	3.6%	4.1%
GDP ($billion)	$406.41	$427.48	$452.14	$473.41	$494.96
Percentage Change		5.2%	5.8%	4.7%	4.6%

The GDP contribution of the franchise industry is predicted to grow by 4.6% in 2020, faster than the U.S. nominal GDP growth rate of 4.1% for 2020 forecasted by the IMF, while the industry's GDP contribution to the total U.S. nominal GDP will remain steady in 2020 at 3%, generating a total of $494.96 billion.



We forecast that most franchise businesses will sustain robust growth in 2020, especially in the personal services, quick service restaurants and full-service restaurants segments, despite tapering growth in the overall U.S. economy.

Personal Services Sector

This sector experienced a surge in recent years, ranked as No. 1 for both franchise establishments and employment growth, and No. 3 for franchise output growth in 2020. The sector's expansion is closely correlated with growth in consumer spending and disposable income, and is mainly driven by brands offering health care and fitness, childcare, and beauty-related services. Brands such as Orangetheory Fitness, Anytime Fitness, Planet Fitness, European Wax Center, The Joint Chiropractic, and Great Clips are found within this sector.

Food Sectors

Food-related franchises are expected to continue to outpace the overall economy in 2020, particularly in the Quick Service Restaurants sector. We forecast this sector will product the most economic output of any of the sectors, while the Table/Full-Service Restaurants sector will rank second among all eight business lines for all franchise establishment, job creation, and output growth. Both sectors are likely to see sales increases from off-premise opportunities, adoption of technology, and healthier menu options reacting to evolving consumer preferences, all of which contributes to their expected growth this year.

Franchised businesses propel our economy not only at the national level, but also at the state level. Our research shows that a business-friendly environment is important for states to support and attract franchising activities, which further bolster employment, output, and GDP growth.

The top ten states for projected franchise establishments and employment growth are, in order: **Texas, Colorado, Arkansas, Florida, Idaho, Tennessee, Georgia, North Carolina, South Carolina, and Nevada.**

Growing populations and pro-business environments mean that **Texas, Colorado, Florida, and North Carolina** are projected to experience growth in franchise establishments, employment, and output.

State-level economic policies will lead to faster franchise establishment and job growth rates for **Tennessee, South Carolina, and Georgia.**

Nevada's favorable business tax climate, **Arkansas**' growing lodging industry, and **Idaho**'s booming technology sector and a low cost of living all result in those states' inclusion in the top ten.

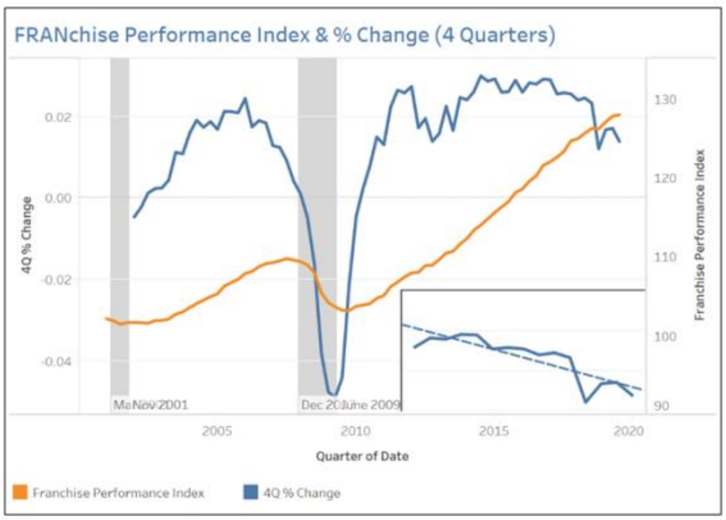
Overall, states in the South and West will continue to expedite the upward trajectory of franchise business development.

Franchise Performance Index

Franchising is an important source of employment and economic output, and it is important to understand the role it plays in the economy. Unfortunately, most franchise data is only reported on an annual basis. To create a timelier measure of franchising's impact on the economy, FRANdata created the FRANchise Performance Index (FPI), a monthly index of franchise activity. The FPI combines six indicators, which FRANdata feels are the best measure of the growth or decline for the franchise business and the general business environment.

The components are as follows:

- Employment in Franchise Businesses (ADP)
- Unemployment Rate (BLS)
- Number of Self-Employed (BLS)
- Retail Sales Performance (Census Bureau)
- Small Business Optimism Index (NFIB)
- Small Business Credit Conditions Index (NFIB)



The FPI, much like the economy as a whole, has been on a positive growth trend since the end of the last recession, but that growth has begun to slow. On the table, the FPI is marked in orange and the percent change (4 quarters difference) is marked in blue.

While the FPI continues to grow, the slope of the growth is clearly tailing off. The inset table shows the percent change from 2016 to YTD 2019, which highlights the slowing growth that franchising has begun to experience.

This trend, as to be expected, is clearly happening to the economy as a whole. Just as with franchising, we see a slowdown in job growth, housing prices, and manufacturing.

FRANchise Performance Index 2019-2020					
	Q1 2019	**Q2 2019**	**Q3 2019**	**Q4 2019**	**Q4 2020**
Index Value	127.1	127.8	128.0	128.8	131.2
Percent Change		0.6%	0.2%	0.6%	1.9%

INTRODUCTION

FRANdata and the International Franchise Association (IFA) created this report as a forecast for the franchise industry of the US economy in 2020. Franchising, employing an estimated 8.4 million people, represents 3% of the total US economy. The franchise model is an important source of economic growth and employment, especially for new entrants to the workforce and those who might lack the educational background for other work.

FRANdata and IFA have organized this report around our forecast for the economy in 2020, with a focus on the economic indicators that relate most directly to franchising. We then present an overview of the impact of franchising for eight business lines:

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

For each of the business lines, FRANdata includes estimates from 2016 to 2019 and a forecast of 2020 of:

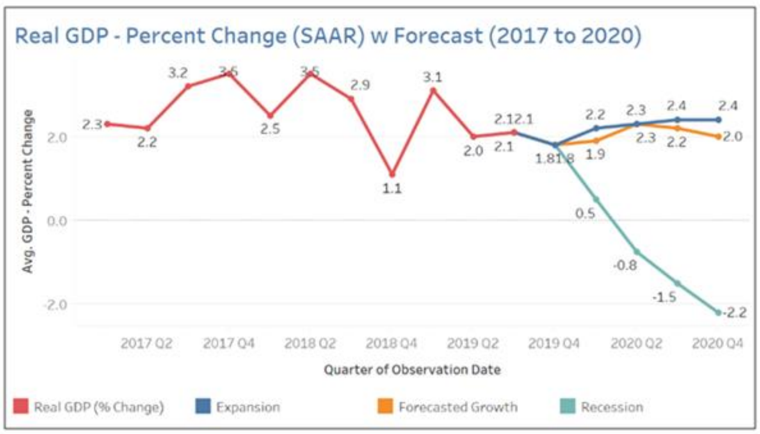
- Franchise Establishments
- Franchise Employment
- Franchise Nominal Output

This report also includes forecasts for franchise growth in each of the 50 states and Washington, D.C. for employment, establishments, payroll, and output.

THE ECONOMIC FORECAST

In 2019, the US economy continued its longest expansion in history, and FRANdata expects the trend of steady but slowing growth to continue. For 2020, FRANdata forecasts continued, but slowing, growth with enough forward movement to avoid recession until 2021.

For franchising, we expect its overall economic output to grow faster than the economy as a whole. While we expect franchising to follow the larger trend of the economy as a whole, we forecast GDP growth of 2.1% for 2020 and expect franchise economic output to grow by almost 4% in 2020. This growth will be driven by increases in the food service (QSR and Sit-down) and personal service sectors.



Economic growth in 2020 will mostly be spurred by consumer spending, increased wages and low unemployment. Unfortunately, there appear to be headwinds in 2020 that could offset those positive forces. Domestically, manufacturing and house prices all show signs of decline. Internationally, global economies are already showing signs of slowing down, and trade issues and tariffs have added drag to the economy[2].

Economic Factors Impacting Franchising

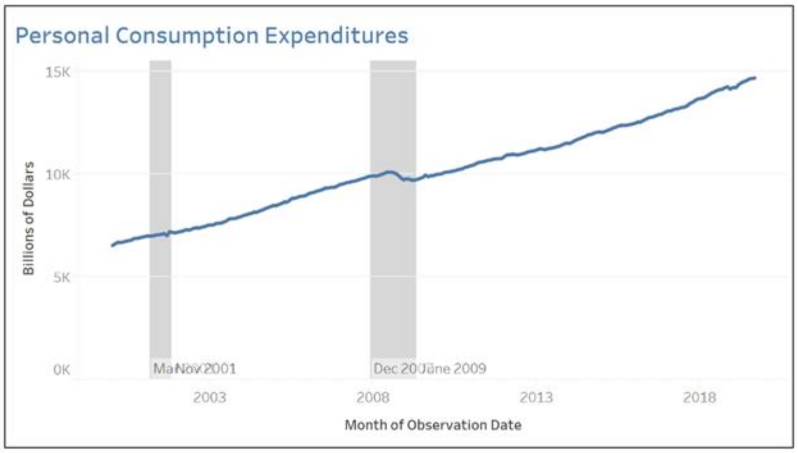
Employment and Wages

Unemployment is currently at the lowest it's been since the 1960s. This is a positive for franchising despite the limited supply of labor. Low unemployment and increasing wages help drive up consumer spending, which benefits franchise concepts, especially the service sectors. The tight labor market also means franchisees have to compete for an increasingly limited labor pool, which has led to an increase in 'job hopping' as employees look for better wages.

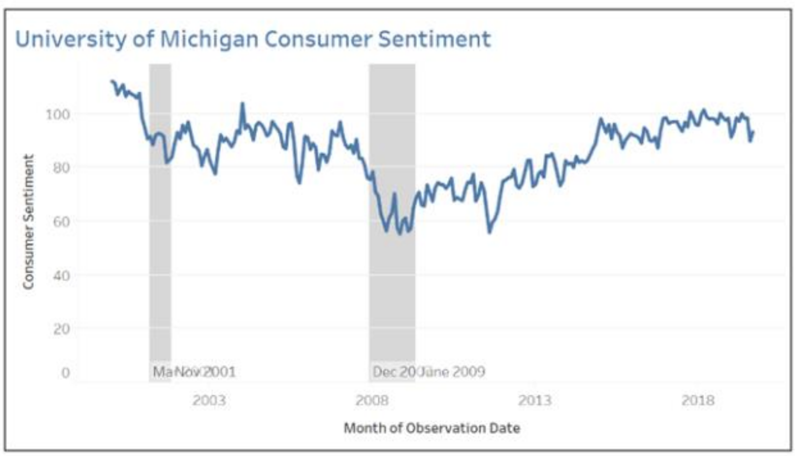
The tight labor market means franchisees have to compete for an increasingly limited labor pool

Consumer Spending & Confidence

US consumer spending has been the engine of the ongoing recovery as it accounts for nearly 70% of the entire economy. Since the end of the last recession, consumer consumption has been on a continuous upward trend, and unlike job growth, this trend shows no signs of slowing. Improving consumer sentiment and consumer spending are both strong positives for franchising, and as long as these factors remain positive, franchising should be well-positioned for success in 2020.



The largest potential risk to consumer spending is increased household debt. In the first quarter of 2017, US household debt surpassed the high which was set before the 2008 recession, and it has continued to grow. Despite this increase in household debt and added credit card and auto debt, new foreclosures and bankruptcies have been on a downward trend.

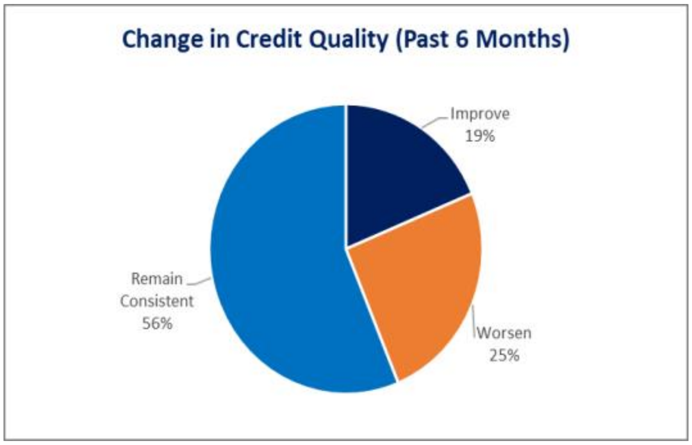


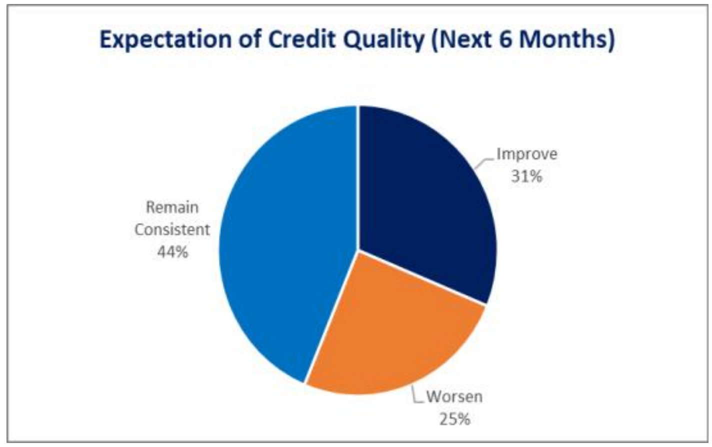
Consumer confidence also continues to improve. In the last two years, consumer confidence has steadily grown at an annual growth rate of 5% in 2019, up from 2.15% in the previous year. Despite an increasing trend, consumer confidence has been volatile, falling from a high of 100 in May to 93 in September. Factors including the perceived economic slowdown, the trade tensions between the US and China, and slower job growth have caused consumers to be less optimistic about the short-term outlook.

Interest Rates & Small Business Lending

As the last recession taught us, capital is the oil that keeps the engine of the economy running smoothly. Any disruption in the flow of capital can have ripple effects throughout the economy. Based on interviews performed with franchise lenders, FRANdata believes that lender expectations are slightly negative. The two most common concerns mentioned include a general recession and an increase in the number of less qualified borrowers. Just over 25% of those interviewed mentioned that they've seen a slight decline in application quality in the last six months and 25% expect to see application quality to continue to decline in the new year. One lender summed this up best when they said, "It looks like a lot of franchisors are having to dig deeper into their pipeline of potential franchisees to meet goals, and that has led to a decrease in the quality."

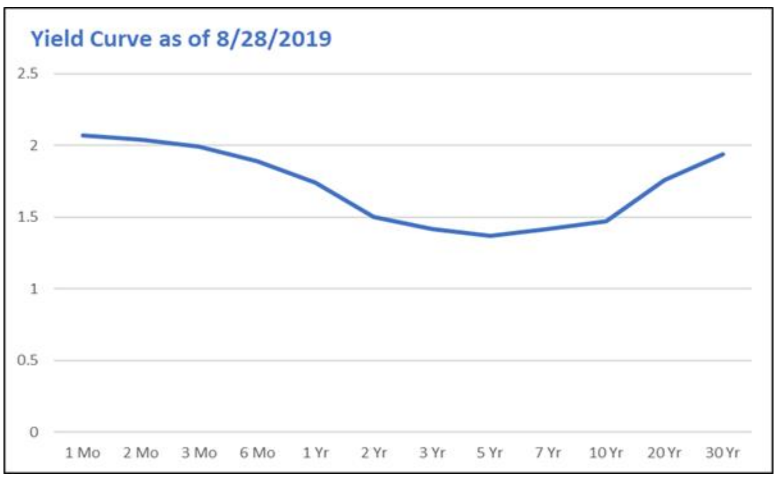
"It looks like a lot of franchisors are having to dig deeper into their pipeline of potential franchisees to meet goals, and that has led to a decrease in the quality"





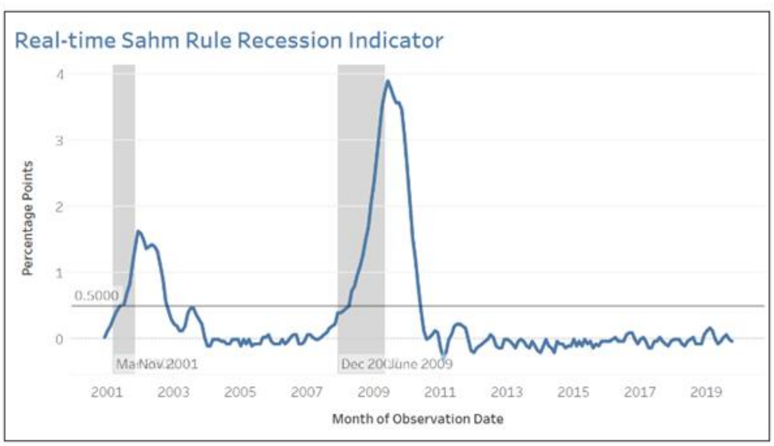
Recession Risks

The economy is an exceptionally complex system, and there are positives and negatives to be found everywhere. The single most concerning warning light for the economy is the inverted yield curve. From August 27th to September 4th, the three-month maturity T-bill had a higher return than the 10-year, which means investors are so worried about the future, they are willing to pay a premium for short-term maturities.



The inverted yield curve has been an accurate predictor of recessions every time it has happened. The timing is less consistent but ranges from two to eight quarters afterward. That means a recession should happen anywhere in 2020 or early 2021.

As the year progresses, FRANdata recommends watching the Sahm Rule Recession Indicator, as it appears to be an excellent measure of identifying when a recession has begun.



The Sahm Rule, created by Claudia Sahm of the Federal Reserve, measures the average three-month unemployment rate. When that rate crosses the .5% line, a recession has begun. This would provide up to six months of advance notice on the traditional identifier of two quarters of negative GDP growth. Currently, the Sahm Rule sits just below zero, but is worth keeping an eye on as it appears to be the earliest possible indicator of a recession beginning.

OUTLOOK FOR FRANCHISE BUSINESS

Outlook Summary

Development in the franchise industry continues to have a significant impact on the U.S. economy. The industry has seen a steady upward trend of franchise establishments and employment in 2019, following 2018's expansion. However, 2020 is expected to have a softer growth, mirroring the overall economic slowdown. In addition, US real GDP is forecast to grow at a slower rate of 2.3% and 2.1% for 2019 and 2020, respectively, compared to the 2.5% growth in 2018[3].

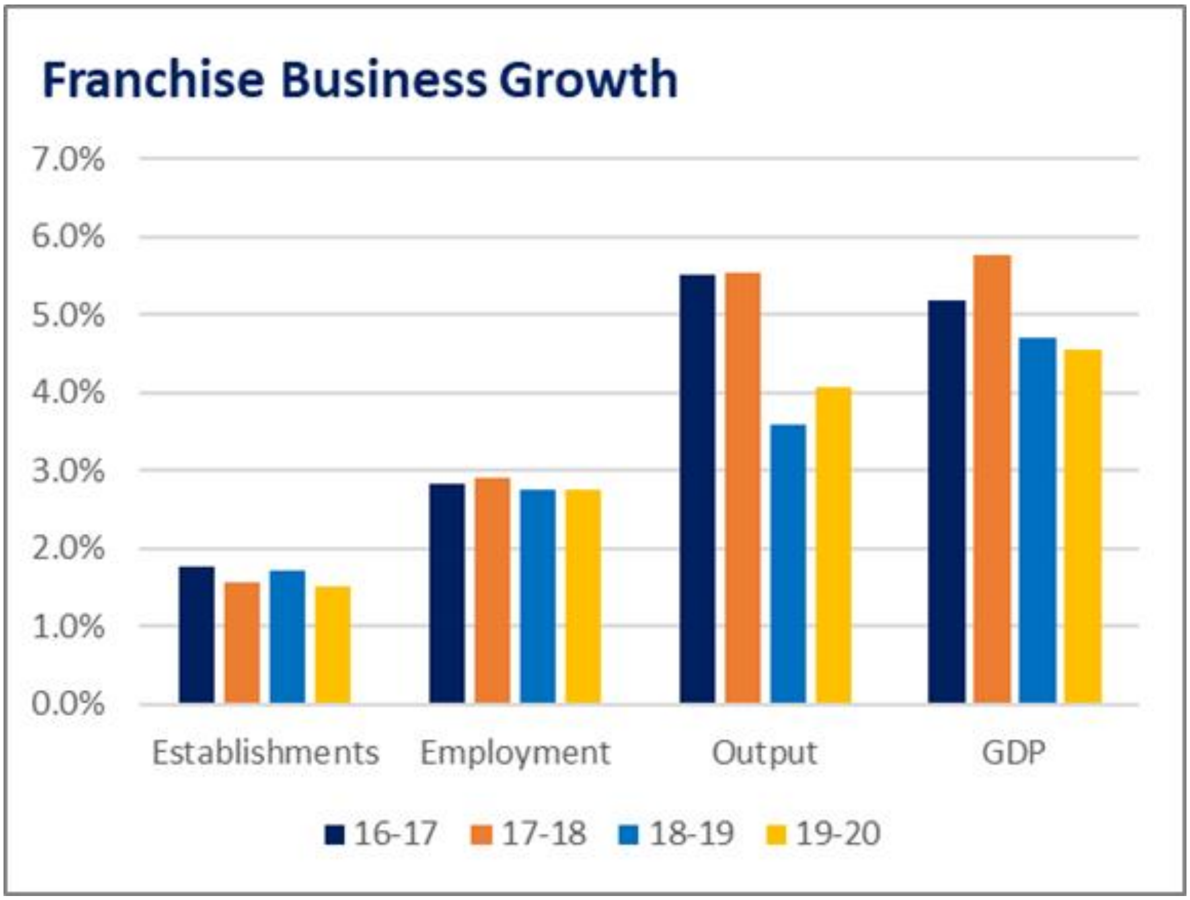
With a low unemployment rate, robust wage growth, and solid consumer spending, franchising should still be equipped with continuous expansion for a majority of the business lines in 2020:

- FRANdata estimates that franchise establishments will increase by 1.5% to 785,316 in 2020. The number of businesses in the Personal Services sector is anticipated to expand at the quickest rate of 4.7% between 2019 and 2020. However, franchises offering business services will undergo a declining trend.
- Franchise employment is projected to increase by 2.8%, growing from approximately 8.4 million to 8.7 million from 2019 to 2020. Jobs added in the Personal Service segment will lead the overall franchise labor market increase, followed by employees hired in the QSR and Table/Full-Service Restaurant segments.
- The output of franchise businesses in nominal dollars is forecast to improve by 4.1% to $819.6 billion in 2020, boosted by revenue growth from QSR and Full-Service Restaurants, as well as Personal Service businesses.
- The franchise industry's GDP contribution to the US total GDP in nominal dollars is predicted to remain stable at 3% in 2020 at $495 billion, a gain of 4.6% from 2019.

Franchise Business Economic Outlook: 2020 Forecast

	Establishments			Employment			Output ($Billion)		
	2019 (Est.)	2020 (Proj.)	Growth Rate	2019 (Est.)	2020 (Proj.)	Growth Rate	2019 (Est.)	2020 (Proj.)	Growth Rate
Business Services	106,936	105,625	-1.2%	650,489	644,540	-0.9%	$106.0	$109.5	3.3%
Commercial & Residential Services	67,226	68,008	1.2%	252,803	255,820	1.2%	$45.8	$46.2	0.8%
Lodging	29,706	30,156	1.5%	662,382	673,398	1.7%	$78.0	$80.3	3.0%
Personal Services	118,825	124,394	4.7%	547,094	580,070	6.0%	$39.3	$41.1	4.5%
Quick Service Restaurants	196,794	199,549	1.4%	3,880,612	4,001,940	3.1%	$267.9	$282.9	5.6%
Real Estate	65,307	65,966	1.0%	262,130	265,787	1.4%	$55.3	$57.3	3.5%
Retail Food, Products & Services	155,649	157,849	1.4%	1,061,686	1,088,696	2.5%	$118.3	$121.8	3.0%
Table/Full Services Restaurants	33,160	33,769	1.8%	1,116,894	1,155,890	3.5%	$76.5	$80.4	5.2%
Total	**773,603**	**785,316**	**1.5%**	**8,434,090**	**8,666,141**	**2.8%**	**$787.5**	**$819.6**	**4.1%**

The following chart shows the historical year-over-year growth of franchise establishments, employment, output, and GDP contribution from 2016 to 2019, and the projected growth rate between 2019 and 2020. Franchise establishments and employment will not be substantially impacted despite the volatility of the current economic condition. Nonetheless, franchise output could be negatively affected due to the hindered growth on franchisee level revenue and profit growth. Consumers are expected to spend more cautiously in the coming months amid a less optimistic attitude toward future economic expansion, and business owners will suffer from increasing inventory and labor costs, which will further suppress franchising activities' GDP contributions to the overall economy through a decelerated growth rate.



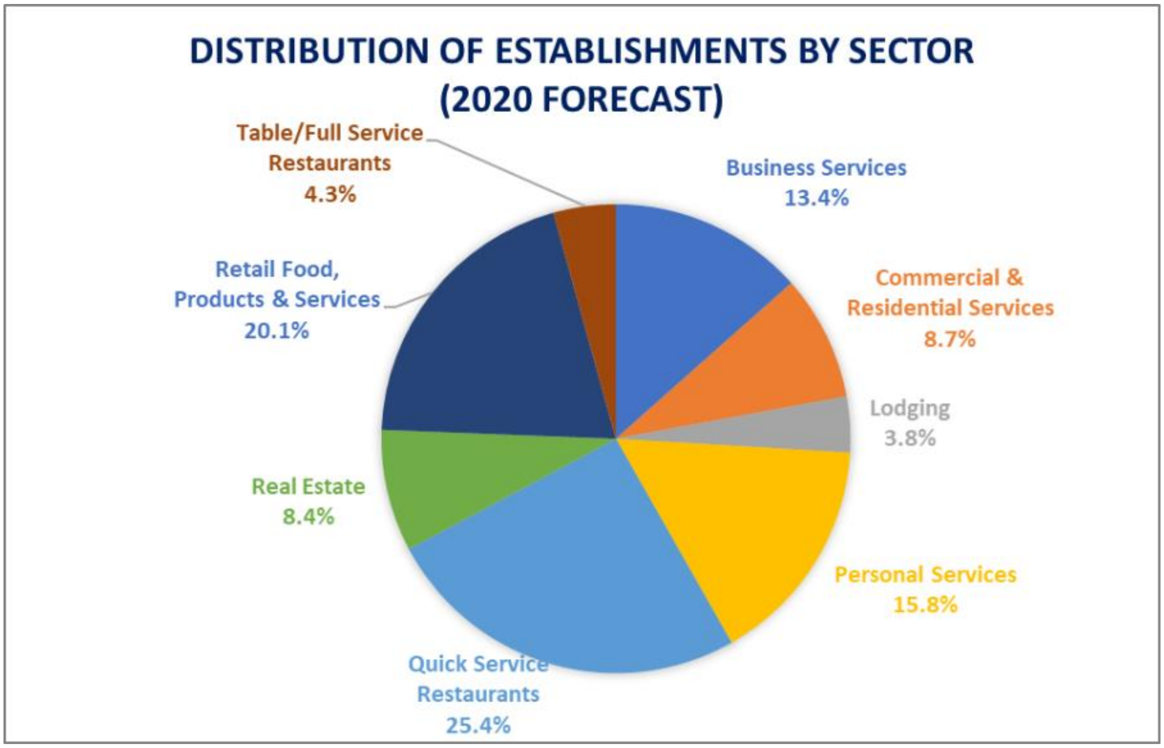
Establishments Growth & Distribution by Business Line

FRANdata estimates that the franchise industry had approximately 773,600 establishments by the end of 2019, up by 1.7% from 2018. Due to uncertainties in the current economic condition, we predict that the total franchise establishments for the eight business lines will increase at a slower rate of 1.5% to approximately 785,300 businesses nation-wide for 2020. The Personal Services business line will experience the fastest growth of 4.7%, driving the overall industry expansion, followed by a 1.8% gain in the Table/Full Service Restaurants sector, and a 1.5% increase in the Lodging sector.

The Quick Service Restaurants(QSR) sector has the largest franchise establishment contribution among the eight business lines, which accounts for 25.4% of the total establishments. The other three largest sectors following in order are Retail Food, Products & Services (20.1%), Personal Services (15.8%), and Business Services (13.4%).

Franchise Establishments by Business Line

	2016	2017	2018	2019 (Est.)	2020 (Proj.)
Business Services	108,172	108,813	108,011	106,936	105,625
Percentage change		0.6%	-0.7%	-1.0%	-1.2%
Commercial & Residential Services	65,114	66,041	66,495	67,226	68,008
Percentage change		1.4%	0.7%	1.1%	1.2%
Lodging	27,450	28,374	29,116	29,706	30,156
Percentage change		3.4%	2.6%	2.0%	1.5%
Personal Services	105,147	109,898	114,058	118,825	124,394
Percentage change		4.5%	3.8%	4.2%	4.7%
Quick Service Restaurants	191,395	192,992	194,395	196,794	199,549
Percentage change		0.8%	0.7%	1.2%	1.4%
Real Estate	61,313	63,098	64,170	65,307	65,966
Percentage change		2.9%	1.7%	1.8%	1.0%
Retail Food, Products & Services	144,516	146,622	151,390	155,649	157,849
Percentage change		1.5%	3.3%	2.8%	1.4%
Table/Full Service Restaurants	32,740	32,914	32,843	33,160	33,769
Percentage change		0.5%	-0.2%	1.0%	1.8%
Total	735,847	748,752	760,476	773,603	785,316
Percentage change		1.8%	1.6%	1.7%	1.5%

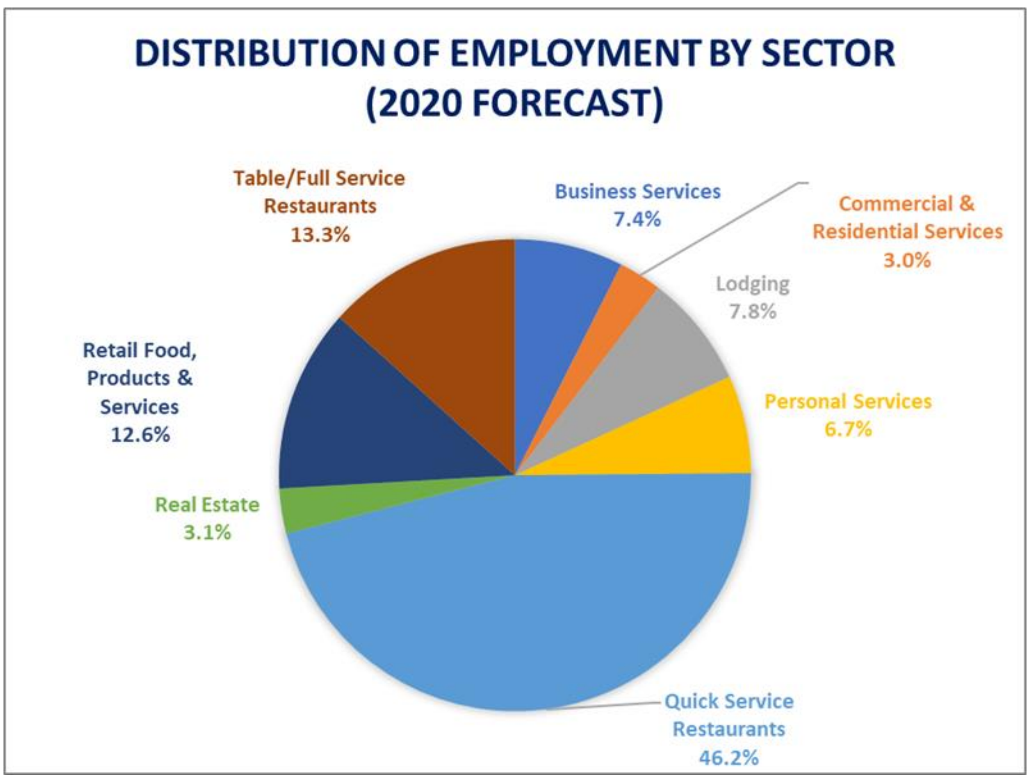


Employment Growth & Distribution by Business Line

FRANdata estimates that the franchise industry added approximately 226,500 jobs in 2019, and franchise employment increased by 2.8% to 8.4 million, maintaining a stable growth rate since 2016. In 2020, total franchise employment is anticipated to rise by 2.8%, through the addition of 232,000 jobs with a sum of 8.7 million employees. Franchise employment growth is mainly expedited by the increasing workers in the Personal Services sector, as that sector also has the fastest business establishment accumulation. Hastened job demand in the QSR and Table/Full Service Restaurants business lines will also promote industry growth by contributing an estimated more than 160,000 jobs.

For the distribution of the eight business lines in terms of franchise employment, the majority of them (46.2%) are from the QSR sector. The second and third largest category are Table/Full Service Restaurants and the Retail Food, Products & Services business lines, which account for 13.3% and 12.6%, respectively.

Franchise Employment by Business Line					
	2016	2017	2018	2019 (Est.)	2020 (Proj.)
Business Services	644,802	651,659	653,999	650,489	644,540
Percentage change		1.1%	0.4%	-0.5%	-0.9%
Commercial & Residential Services	244,251	247,415	250,318	252,803	255,820
Percentage change		1.3%	1.2%	1.0%	1.2%
Lodging	606,168	627,354	648,806	662,382	673,398
Percentage change		3.5%	3.4%	2.1%	1.7%
Personal Services	460,390	490,915	519,369	547,094	580,070
Percentage change		6.6%	5.8%	5.3%	6.0%
Quick Service Restaurants	3,561,108	3,659,560	3,770,426	3,880,612	4,001,940
Percentage change		2.8%	3.0%	2.9%	3.1%
Real Estate	242,702	251,046	256,328	262,130	265,787
Percentage change		3.4%	2.1%	2.3%	1.4%
Retail Food, Products & Services	953,009	977,712	1,020,002	1,061,686	1,088,696
Percentage change		2.6%	4.3%	4.1%	2.5%
Table/Full Service Restaurants	1,043,772	1,069,518	1,088,352	1,116,894	1,155,890
Percentage change		2.5%	1.8%	2.6%	3.5%
Total	**7,756,202**	**7,975,179**	**8,207,599**	**8,434,090**	**8,666,141**
Percentage change		**2.8%**	**2.9%**	**2.8%**	**2.8%**



Output Growth & Distribution by Business Line

We forecast that franchise output, which represents sales of all the franchise businesses on the aggregated level, rose by 3.6% to $787.5 billion in 2019 and will improve at a slightly faster pace of 4.1% to $819.6 billion in 2020. We project that the steady growth and expansion coming from the industry leaders, the QSR and Table/Full Service Restaurants sectors, will amplify the output production. Meanwhile, the expansion of the Personal Services sector is also expected to reinforce revenues induced from the overall franchise businesses.

2020 Growth Predictions

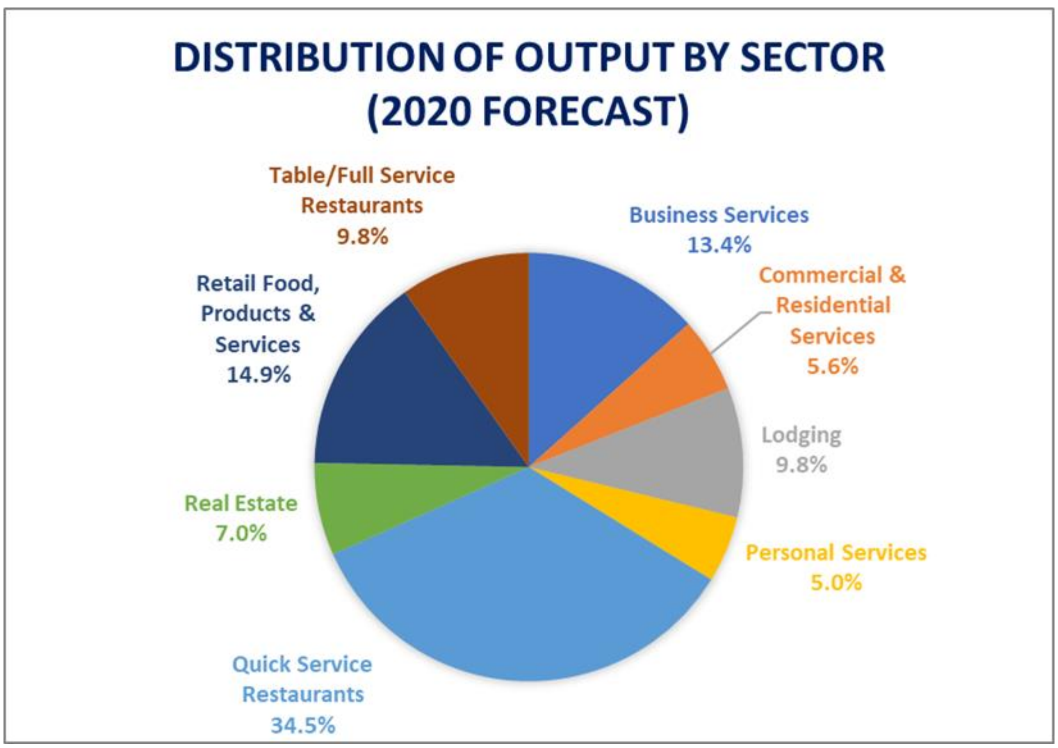
Franchise Output 4.1% to $819.6 billion

Business Service Sector 3.3% growth

The Business Service sector is predicted to experience a 3.3% growth in output in 2020, which makes it the fifth ranked contributor among the eight business lines, even though the sector has experienced a downward trend on franchise establishments and employment. We presume the upward trend in the Business Service sector's growth is due to the existing businesses continuing their persistent sales growth. As clientele are establishing along with the length of operation history, operators in this segment will have accelerated recurring revenue. Therefore, this sector also has a higher level of output per establishment and per employee.

Similar to the franchise employment, the QSR business line also provides the highest proportion to the total franchise output among the eight business lines, at 34.5%. The Retail Food, Products & Services and Business Services business lines rank second and third, comprising 14.9% and 13.4% of the total franchise output, respectively.

Franchise Output by Business Line ($Billion)					
	2016	2017	2018	2019 (Est.)	2020 (Proj.)
Business Services	$94.2	$98.2	$103.1	$106.0	$109.5
Percentage change		4.3%	5.0%	2.8%	3.3%
Commercial & Residential Services	$42.6	$43.9	$45.5	$45.8	$46.2
Percentage change		3.0%	3.6%	0.7%	0.8%
Lodging	$68.4	$71.7	$75.7	$78.0	$80.3
Percentage change		4.8%	5.6%	3.0%	3.0%
Personal Services	$33.3	$35.6	$37.9	$39.3	$41.1
Percentage change		7.1%	6.3%	3.8%	4.5%
Quick Service Restaurants	$225.7	$240.5	$256.6	$267.9	$282.9
Percentage change		6.5%	6.7%	4.4%	5.6%
Real Estate	$48.3	$50.9	$53.4	$55.3	$57.3
Percentage change		5.6%	4.8%	3.7%	3.5%
Retail Food, Products & Services	$106.3	$111.1	$115.1	$118.3	$121.8
Percentage change		4.5%	3.7%	2.8%	3.0%
Table/Full Service Restaurants	$64.0	$68.5	$73.0	$76.5	$80.4
Percentage change		7.1%	6.6%	4.8%	5.2%
Grand Total	**$682.7**	**$720.4**	**$760.3**	**$787.5**	**$819.6**
Percentage change		**5.5%**	**5.5%**	**3.6%**	**4.1%**



Business Lines Overview

FRANdata is able to break down the franchise industry into eight major business lines, all of which have significant franchising activities. By having a broad overview of each business line's forecasted growth tendency for 2020, we expect Personal Services, QSR and Full-Service Restaurants to be the top business lines that propel industry growth.

Personal Services:

The Personal Services business line includes diverse services ranging from education, health and fitness, entertainment and recreation, beauty salons, massage and spa, veterinarians, and personal finances. This segment is closely linked to changes in per capita disposable income and consumer spending, which both grew at a steady pace. Personal income gained $50.2 billion in September of 2019, up 0.3% from just a month before. Personal consumption expenditures also expanded, increasing by 0.2% to $24.3 billion in September, following the same growth in August[4].

The Personal Services segment had a surge over the last few years, and the sector is expected to be placed first for growth among the eight business lines, both in terms of the number of establishments and employment. We estimated that the franchised units in Personal Services increased by 4.2% in 2019 and will grow at a faster rate of 4.7% in 2020 to a total of 124,394 businesses. Among the personal services, brands in the healthcare, beauty-related and child-related services, such as Orangetheory Fitness, Anytime Fitness, Planet Fitness, European Wax Center, The Joint Chiropractic, and Great Clips, have experienced extensive growth for the past three years, and are forecast to continue the upward trend in 2020. Franchise employment is projected to grow robustly at 6% by adding a total of 32,976 jobs to approximately 580,000 employees working in the sector. 2020 will see continuing improvement by creating $41.1 billion in output, at a rate of 4.5%, which is third among all business lines. This is an improvement over the 3.8% in the year prior.

Quick Service Restaurants:

The Quick Service Restaurants segment has experienced dynamic changes over the past three years, offering increasingly healthier food options and innovative menu items in response to changing consumer tastes. This sector has also continued its growth by adopting new technology and embracing off-premises opportunities. We expect the QSR sector to maintain its upward trajectory in 2019 and 2020, facilitated by the popularity of fast-casual restaurants. As personal consumption expenditure remains high, consumers are more likely to eat out, which will also benefit the sector as a whole. Even during an economic recession, consumer demand for low-priced food offerings will spur this segment's growth to prevent severe profit loss. However, because of labor shortage and increasing labor costs, in addition to a potential hike in supply costs as a result of the trade war between the US and China, the sector may face potential threats as it expands.

The number of franchise establishments for the QSR sector has seen an accelerated growth of 1.2% for 2019, up from 0.7% in 2018. 2020 is forecast to see a slightly higher rate of 1.4%, tying it for fourth among the business lines, with a total of 199,549 businesses. We estimate that employment has improved 2.9% in 2019 and will increase 3.1% in 2020 to approximately 4 million workers providing services in the sector, placing the segment in the third position in terms of growth rate. Franchise output for franchise businesses in the sector grew at a reduced rate of 4.4% for 2019, compared to the 6.7% growth rate in 2018. This slowdown could possibly be due to hindered revenue growth generated at the franchisee level under the current unfavorable economic condition. However, in 2020, we expect the segment will expand at the rate of 5.6% to $282.9 billion without any further decline. The growth will rank the sector highest among the eight business lines, which will lead the franchise industry's overall output development.

Table/Full-Service Restaurants:

The Table/Full-Service Restaurant sector has seen sluggish growth in 2017 and 2018, amid the changing millennial consumer preferences and food habits. However, the sector was able to rebound in 2019, where the total number of franchise establishments grew by 1% the same year, and is expected to experience accelerated growth in 2020 at a rate of 1.8% to a total of 33,769 locations, ranking second in regards to growth rate. As consumers have begun to be more health conscious and pursue better quality foods with fresh ingredients under comfortable dining environments, the traditional family-style casual dining restaurants may seek innovations for growth opportunities. Operators in the sector have started seeing higher sales with off-premise dining. Restaurants such as Texas Roadhouse and First Watch, which offer specialized dining services, have experienced improving performances as well.

The rise in consumer spending, wage growth and low unemployment are all favorable to the growth of this sector, which added an estimated 28,600 jobs in 2019, and is predicted to add approximately 39,000 more jobs in 2020, with more than 1.2 million hired in the sector. The 3.5% employment growth for 2020 ranks the sector second among the eight business lines, facilitating the overall franchise industry job creation. Meanwhile, we project output growth in the Table/Full-Service Restaurant segment to increase from 4.8% in 2019 to 5.2% in 2020, generating $80.4 billion in total sales. This still places the sector in second position among the eight business lines, which is also one of the main forces that will expedite the franchise industry's output expansion.

Lodging:

Franchise establishment in the Lodging segment is expected to continue expanding at an annual growth rate of 1.5% in 2020 to 30,156, down from 2.0% in 2019. The growth rate places the sector third among the eight business lines and is in line with the broader franchise industry growth rate. Holiday Inn and Hampton Inn by Hilton had the most franchised units among lodging brands, reaching more than 2,000 units in 2018. We have also seen an increasing number of new brands beginning to offer franchises in this segment, such as Destination Hotels by Hyatt, Signia by Hilton, Everhome Suites by Choice, and Atwell Suites by Intercontinental.

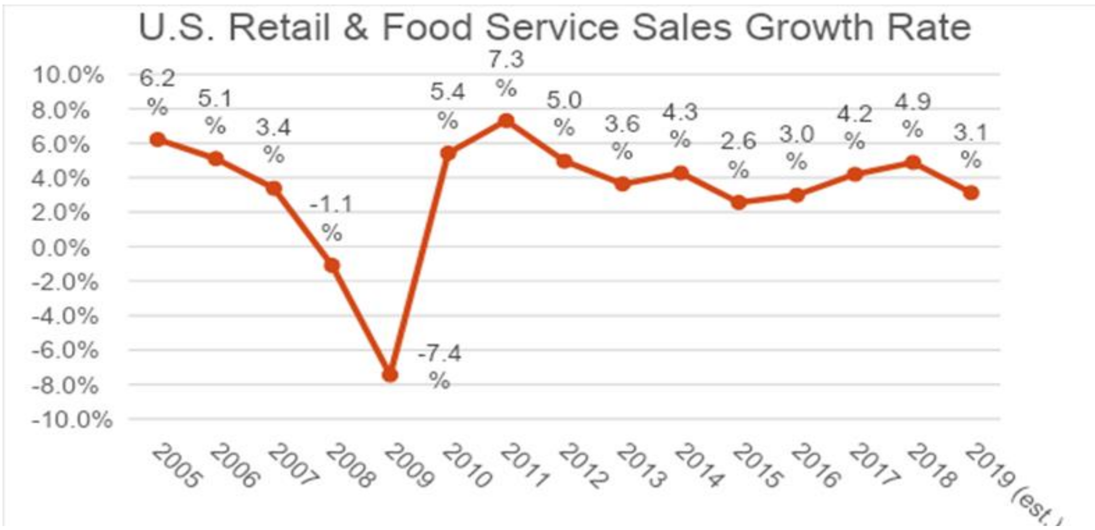
Job growth will continue, but may experience a slower momentum in 2020, primarily due to declining labor force participation rates and competitive hiring within other industries[5]. Franchise employment is expected to grow at a rate of 1.7%, fifth among all business lines, adding more than 11,000 jobs with a projected total of 673,000 employees working in the sector.

Despite being affected by the volatile global economy, the output growth in the Lodging sector has been robust in the past four years. As the risk of economic slowdown and trade tensions rise, we estimate the output growth will increase at a lingering pace of 3% in 2020 to $80.3 billion, ranking it sixth among the eight business lines.

Retail Food, Products & Services:

Bolstered by a strong labor market, a rise in disposable personal income and elevated consumer confidence, 2018 experienced strong retail sales[6], which has also positively influenced the franchise industry. The total franchise establishments in this segment increased to 151,390 in 2018, at a growth rate of 3.3%.

In 2019, we have seen shakes in consumer confidence, an alleviated impact of tax cuts on income, and potential pricing pressure on food and products due to the trade war, which means that the US retail and goods services sales are estimated to grow at a lower rate of 3.1% in 2019 after a 4.9% growth in 2018. FRANdata anticipates this number of franchise businesses in the Retail Food, Products & Services sector will follow a similar descent with the overall US retail & food service sales growth rate by increasing at an estimated lower rate of 2.8% in 2019 and a projected rate of 1.4% in 2020. This fourth-fastest growing sector is expected to retain more than 157,100 business establishments. According to CNBC, for every 1% increase in online sales, roughly 8,000 to 8,500 stores will shutter, particularly clothing retailers, consumer electronics companies and home furnishing businesses[7]. Therefore, the rising popularity of online shopping and e-commerce has also had an adverse effect on physical retail locations, which is one of the reasons for the restrained growth of franchise establishments



Employment in the franchise Retail Food, Products & Services sector grew an estimated 4.1% in 2019, and is forecast to improve by 2.1% in 2020 with up to 1.1 million employees, placing it fourth among overall business lines. Output is expected to increase by 3.0% in 2020 to $121.8 billion, up from 2.8% in 2019, ranking it sixth in respect to growth rate.

Real Estate:

The franchise Real Estate sector is strongly correlated with the residential and commercial real estate market. The US housing market has made a slow but steady recovery since the recession. However, 2019 has seen lukewarm home price growth rates, with a decline in existing home sales[8], along with curtailed business investment activities. Therefore, FRANdata expects the sector to have a lagging growth rate of 1% on franchise establishments for 2020 to approximately 65,970 businesses, compared to a 1.8% growth in 2019, which ranks it seventh among the eight business lines. Brands providing real estate brokerage and services will lead the sector's growth, as increasing per capita disposable income and historically low interest rates will reinforce home affordability. This will momentarily underpin demand for real estate agents and brokers. We also expect to see more brands offering coworking/shared office services and meeting room facilities, such as Office Evolution, Venture X, Serendipity Labs, and Intelligent Office.

Franchise employment growth for the Real Estate sector is predicted to slow from 2.3% in 2019 to 1.4% in 2020 by having approximately 265,800 employees, making it sixth among all business lines, while output has grown moderately at 3.7% in 2019 and will increase by 3.5% to $57.3 billion in 2020, making it fourth among the business lines.

Business Services:

In 2020, the total number of franchise establishments in the Business Services segment is expected to decrease by 1.2% to 105,600, ranking lowest among the eight business lines in terms of growth rate. Franchise employment is forecast to decline to 644,540 employees working in the sector, at a rate of -0.9%, also ranking the lowest. However, franchise output will see a moderate growth rate of 3.3% to $109.5 billion, placing it fifth among eight business lines.

FRANdata estimates that the downward trend in this segment's establishment and employment growth is primarily affected by brands offering tax and printing services, including H&R Block and Jackson Hewitt Tax Service, as these companies control large market shares, which have encountered restrained development opportunities since 2018. With the impact of tax cuts diminishing in 2020, jobs added in the tax preparation sector are also forecast to undergo a tepid growth. On the other hand, franchises that offer insurance products and services, personnel services, mailing, packaging, and shipping services in the segment will see an accelerated growth rate. Even though the number of franchise establishments in this sector is expected to decrease, franchise output is estimated to see an upward trend, which could be the consequence of existing businesses' recurring revenue growth from established and accumulated client bases.

Commercial & Residential Services:

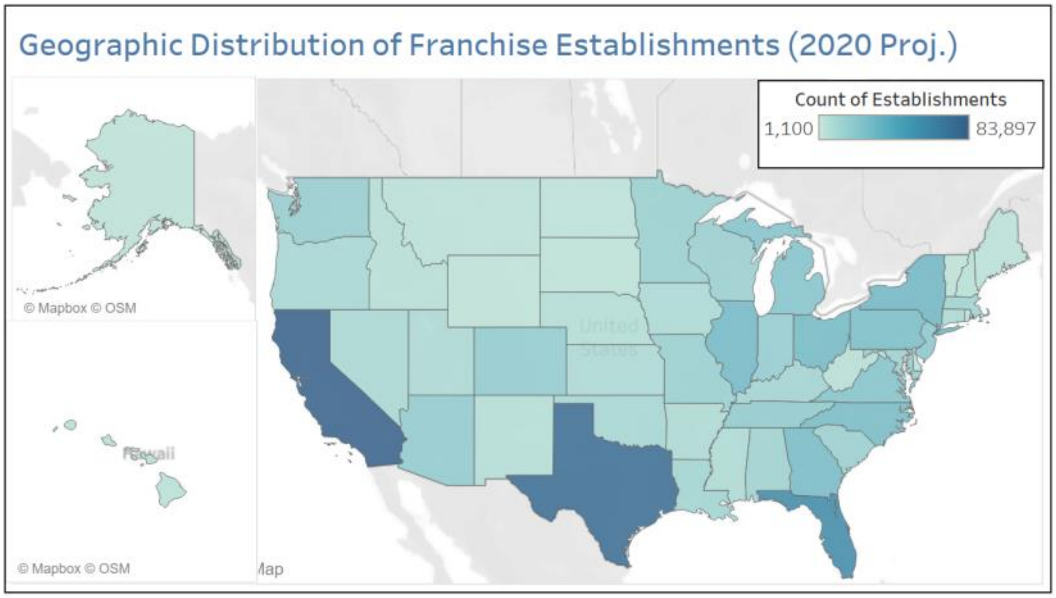
Growth in franchise establishments in the Commercial & Residential Services business line is projected to increase at a rate of 1.2% in 2020, slightly up from 1.1% in 2019, to approximately 68,000 businesses, ranking sixth among eight business lines. In turn, employment from these types of services is also expected to increase at a faster rate of 1.2% in 2020, compared to 1% in 2019, adding 3,000 jobs to a total of 255,800 employees in the segment. However, the sector's output growth is predicted to grow at the lowest rate of 0.8% among the eight business lines, to $46.2 billion in 2020.

The Commercial and Residential Services could be impacted significantly by lower business investments and impassive growth in the housing market. As small business owners have less optimistic outlooks for future investment environments, business owners will feel inhibited from investing in new businesses as well as renovating or remodeling their existing businesses.

State-Level Franchise Outlook

State Overview

Franchising plays an important role at both the national level and the state level. Franchise businesses influence state economies through job creation, promotion of output, and GDP contribution. It is important for states to provide a favorable business environment to support and attract a large franchising community.



FRANdata has found that state level franchise establishments are largely driven by state population, as a high population density area will provide an adequate labor force as well as higher-quality potential franchisees, and a substantially higher consumer demand. California, Texas, Florida, New York, Illinois, Ohio, Georgia, North Carolina, Pennsylvania, and Michigan are the top 10 states with the highest franchise establishments, corresponding to states with the highest populations[9]. At the same time, states offer different levels of appeal from an economic, regulatory, and tax standpoint for franchises that could also potentially impact franchise growth.

In 2020, 25 states and Washington D.C. will raise their minimum wages[10]. A higher minimum wage could place pressure on operators to maintain stable profit margins. Small business owners may need to increase the prices of their service offerings to offset the increased labor costs or hire fewer employees, which will likely have the most negative effects on low-skilled workers. For states that have not adopted a state minimum wage or have minimum wage below the federal minimum wage, such as Tennessee, South Carolina, and Georgia, we expect to see a faster franchise establishment and job growth rate for 2020.

Other than the aforementioned states, FRANdata estimates that Texas, Colorado, Florida, and North Carolina will continue to have the highest franchise establishment, employment, and output growth for 2020, as these states' economic expansions will be expedited and continuously benefit from the influx of new residents. Nevada has also seen significantly higher franchising activities on job and output growth, mainly in the Maintenance Services and Health and Fitness industries. Based on the 2020 State Business Tax Climate Index, Nevada ranked No. 7 among all the states in the US without corporate or individual income tax, which could attract business investments.

Idaho and Arkansas are among the top states for franchise growth as well. Arkansas' employment and output growth are propelled by the lodging industry. Idaho has seen businesses added in Leisure and Food, as well as Health and Fitness. According to the data published by the US Census Bureau, Idaho has earned the title of fastest-growing state of 2018, driven by the 2.1% growth in population. The expansion of Idaho is also facilitated by the booming technology industry, based in Idaho's capital of Boise, and the lower cost of living.

Due to the estimated slower economic growth rate for 2020 and potential shrinking in population[11], we project that states in the northeast, such as Maine, Vermont, Connecticut, and Rhode Island, will have a declining trend on franchise establishments with fewer jobs created.

Top 10 States for Franchise Growth: 2019-2020			
Employment		Output	
State	Growth Rate	State	Growth Rate
TEXAS	5.3%	TEXAS	7.1%
COLORADO	3.9%	FLORIDA	5.3%
ARKANSAS	3.8%	ARKANSAS	5.2%
FLORIDA	3.8%	COLORADO	5.2%
IDAHO	3.6%	NEVADA	4.9%
TENNESSEE	3.5%	NORTH CAROLINA	4.8%
GEORGIA	3.5%	IDAHO	4.8%
NORTH CAROLINA	3.4%	SOUTH CAROLINA	4.7%
SOUTH CAROLINA	3.4%	WASHINGTON	4.7%
NEVADA	3.4%	GEORGIA	4.6%

"California has recently passed Assembly Bill 5 (AB5) in September of 2019 to classify independent contractors as employees, effective January 2020. This may impact franchisors and franchisees' relationships, as well as franchisees and their employees' relationships, which could change franchisors' approaches in franchising in California"

Several litigations should also be monitored in 2020. California has recently passed Assembly Bill 5 (AB5) in September of 2019 to classify independent contractors as employees, effective January 2020. This may impact franchisors and franchisees' relationships, as well as franchisees and their employees' relationships, which could change franchisors' approaches in franchising in California. At the same time, the California Consumer Privacy Act (CCPA), which also goes into effect January 1, 2020, could govern how franchisors and franchisees collect, share, and use consumers' personal information to create business opportunities. While the two Acts are only now applicable in the state of California, at least 12 other states (Hawaii, Illinois, Maryland, Massachusetts, Minnesota, New Jersey, New Mexico, New York, Pennsylvania, Rhode Island, Texas, and Washington State) are considering new privacy bills similar to the CCPA[12], and Washington and New York are also working on their own versions of AB5 bills[13].

Overall, a state's success can be contributed to its growing population, lower costs of living and business-friendly environments. We expect to see continuous business expansion in most states in 2020, with solid job creation and output growth.

Franchising Activity by State

	Franchise Establishments			Franchise Employment		
State	2019	2020	Growth Rate	2019	2020	Growth Rate
ALABAMA	12,705	12,921	1.7%	135,181	139,149	2.9%
ALASKA	1,301	1,298	-0.2%	10,830	10,934	1.0%
ARIZONA	17,867	18,176	1.7%	196,222	202,041	3.0%
ARKANSAS	7,109	7,288	2.5%	74,841	77,655	3.8%
CALIFORNIA	82,623	83,897	1.5%	826,637	849,592	2.8%
COLORADO	16,917	17,364	2.6%	169,739	176,341	3.9%
CONNECTICUT	7,620	7,549	-0.9%	93,113	93,376	0.3%
DELAWARE	2,344	2,379	1.5%	26,381	27,105	2.7%
DISTRICT OF COLUMBIA	1,367	1,408	2.9%	22,437	23,389	4.2%
FLORIDA	57,573	59,017	2.5%	654,222	678,789	3.8%
GEORGIA	27,753	28,389	2.3%	300,183	310,798	3.5%
HAWAII	3,073	3,107	1.1%	52,964	54,204	2.3%
IDAHO	4,136	4,234	2.3%	41,599	43,096	3.6%
ILLINOIS	29,791	29,854	0.2%	349,387	354,388	1.4%
INDIANA	16,545	16,714	1.0%	197,196	201,624	2.2%
IOWA	8,161	8,279	1.4%	81,805	83,996	2.7%
KANSAS	7,965	8,067	1.3%	81,002	83,030	2.5%
KENTUCKY	10,792	10,907	1.1%	129,199	132,160	2.3%
LOUISIANA	11,280	11,455	1.6%	119,253	122,576	2.8%
MAINE	2,540	2,485	-2.1%	25,191	24,954	-0.9%
MARYLAND	14,067	14,073	0.0%	162,989	165,038	1.3%
MASSACHUSETTS	12,533	12,416	-0.9%	122,067	122,397	0.3%
MICHIGAN	22,539	22,733	0.9%	248,395	253,586	2.1%
MINNESOTA	15,141	15,175	0.2%	158,428	160,718	1.4%
MISSISSIPPI	6,611	6,680	1.0%	67,410	68,941	2.3%
MISSOURI	15,099	15,254	1.0%	166,093	169,847	2.3%
MONTANA	2,936	2,975	1.3%	24,980	25,619	2.6%
NEBRASKA	5,694	5,799	1.9%	57,774	59,566	3.1%
NEVADA	8,277	8,454	2.1%	103,553	107,050	3.4%
NEW HAMPSHIRE	3,287	3,275	-0.4%	29,896	30,147	0.8%
NEW JERSEY	19,571	19,720	0.8%	204,280	208,347	2.0%
NEW MEXICO	4,895	4,921	0.5%	57,337	58,352	1.8%
NEW YORK	30,395	30,285	-0.4%	331,856	334,674	0.8%
NORTH CAROLINA	27,477	28,083	2.2%	338,687	350,362	3.4%
NORTH DAKOTA	2,412	2,433	0.9%	28,095	28,691	2.1%
OHIO	28,771	29,150	1.3%	351,267	360,218	2.5%
OKLAHOMA	9,837	10,006	1.7%	97,827	100,719	3.0%
OREGON	9,433	9,537	1.1%	89,165	91,241	2.3%
PENNSYLVANIA	26,626	26,745	0.4%	281,340	286,039	1.7%
RHODE ISLAND	2,230	2,208	-1.0%	20,099	20,143	0.2%
SOUTH CAROLINA	14,071	14,375	2.2%	154,595	159,843	3.4%
SOUTH DAKOTA	2,717	2,738	0.8%	24,100	24,583	2.0%
TENNESSEE	18,227	18,645	2.3%	218,065	225,786	3.5%
TEXAS	73,644	76,607	4.0%	784,216	825,687	5.3%
UTAH	7,989	8,106	1.5%	80,909	83,096	2.7%
VERMONT	1,122	1,100	-2.0%	8,759	8,687	-0.8%
VIRGINIA	22,512	22,613	0.5%	250,202	254,385	1.7%
WASHINGTON	16,070	16,408	2.1%	157,741	163,015	3.3%
WEST VIRGINIA	3,583	3,564	-0.5%	35,005	35,247	0.7%
WISCONSIN	14,616	14,673	0.4%	158,649	161,197	1.6%
WYOMING	1,757	1,778	1.2%	32,928	33,722	2.4%

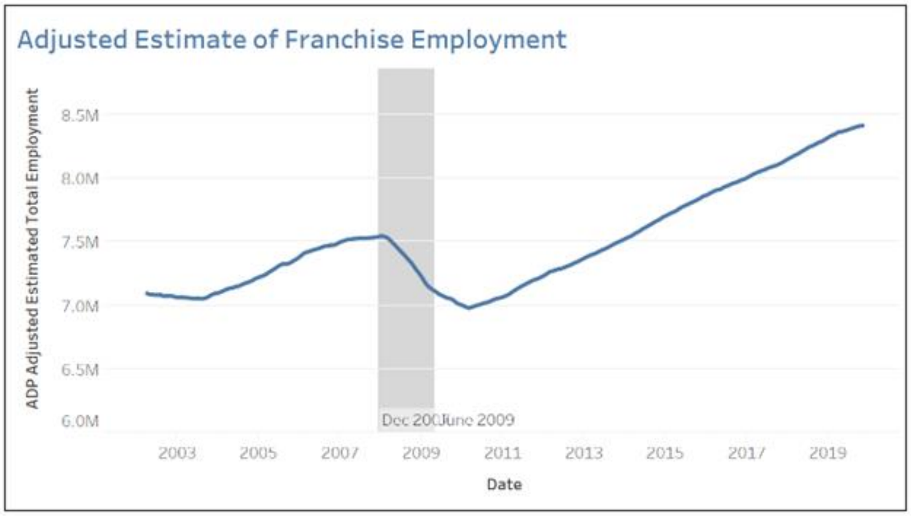
	Franchise Output (in million $)			Franchise Payroll (in million $)		
State	2019	2020	Growth Rate	2019	2020	Growth Rate
ALABAMA	$10,898	$11,312	3.8%	$4,267	$4,487	5.1%
ALASKA	$1,170	$1,201	2.6%	$498	$514	3.3%
ARIZONA	$18,334	$19,134	4.4%	$7,422	$7,821	5.4%
ARKANSAS	$5,945	$6,255	5.2%	$2,235	$2,372	6.1%
CALIFORNIA	$82,944	$86,474	4.3%	$35,319	$37,400	5.9%
COLORADO	$15,896	$16,721	5.2%	$6,534	$6,986	6.9%
CONNECTICUT	$10,794	$10,994	1.9%	$4,934	$5,044	2.2%
DELAWARE	$2,870	$2,991	4.2%	$1,150	$1,206	4.8%
DISTRICT OF COLUMBIA	$3,386	$3,549	4.8%	$1,638	$1,728	5.5%
FLORIDA	$60,286	$63,497	5.3%	$24,670	$26,465	7.3%
GEORGIA	$25,711	$26,895	4.6%	$10,538	$11,196	6.2%
HAWAII	$6,209	$6,421	3.4%	$2,601	$2,710	4.2%
IDAHO	$3,142	$3,291	4.8%	$1,191	$1,268	6.4%
ILLINOIS	$35,764	$36,584	2.3%	$14,750	$15,296	3.7%
INDIANA	$15,674	$16,189	3.3%	$5,911	$6,168	4.3%
IOWA	$6,887	$7,179	4.2%	$2,532	$2,690	6.3%
KANSAS	$6,801	$7,047	3.6%	$2,664	$2,798	5.0%
KENTUCKY	$9,777	$10,080	3.1%	$3,866	$4,039	4.5%
LOUISIANA	$10,612	$11,057	4.2%	$4,127	$4,341	5.2%
MAINE	$2,276	$2,281	0.3%	$868	$875	0.9%
MARYLAND	$16,442	$16,900	2.8%	$6,973	$7,277	4.4%
MASSACHUSETTS	$13,200	$13,415	1.6%	$5,499	$5,679	3.3%
MICHIGAN	$20,026	$20,561	2.7%	$7,489	$7,812	4.3%
MINNESOTA	$14,576	$14,962	2.6%	$5,717	$5,917	3.5%
MISSISSIPPI	$5,482	$5,667	3.4%	$2,133	$2,248	5.4%
MISSOURI	$14,476	$15,000	3.6%	$5,740	$6,062	5.6%
MONTANA	$2,067	$2,147	3.8%	$787	$834	6.0%
NEBRASKA	$5,180	$5,412	4.5%	$1,973	$2,094	6.1%
NEVADA	$11,003	$11,543	4.9%	$4,562	$4,826	5.8%
NEW HAMPSHIRE	$3,016	$3,086	2.3%	$1,225	$1,270	3.6%
NEW JERSEY	$22,705	$23,413	3.1%	$9,168	$9,586	4.6%
NEW MEXICO	$4,685	$4,817	2.8%	$1,815	$1,899	4.7%
NEW YORK	$40,018	$41,196	2.9%	$17,333	$18,040	4.1%
NORTH CAROLINA	$29,425	$30,842	4.8%	$12,190	$12,921	6.0%
NORTH DAKOTA	$3,199	$3,313	3.6%	$1,159	$1,207	4.2%
OHIO	$28,896	$29,969	3.7%	$11,870	$12,516	5.4%
OKLAHOMA	$8,106	$8,472	4.5%	$3,269	$3,483	6.5%
OREGON	$8,258	$8,592	4.0%	$3,403	$3,589	5.5%
PENNSYLVANIA	$26,771	$27,528	2.8%	$10,873	$11,339	4.3%
RHODE ISLAND	$2,153	$2,189	1.7%	$852	$880	3.4%
SOUTH CAROLINA	$12,753	$13,355	4.7%	$4,929	$5,232	6.2%
SOUTH DAKOTA	$2,025	$2,096	3.5%	$701	$731	4.3%
TENNESSEE	$19,139	$20,019	4.6%	$7,808	$8,281	6.1%
TEXAS	$69,693	$74,644	7.1%	$28,909	$31,472	8.9%
UTAH	$6,805	$7,096	4.3%	$2,801	$2,988	6.7%
VERMONT	$861	$866	0.6%	$323	$331	2.7%
VIRGINIA	$23,190	$23,877	3.0%	$9,598	$10,011	4.3%
WASHINGTON	$16,822	$17,608	4.7%	$6,699	$7,136	6.5%
WEST VIRGINIA	$2,751	$2,800	1.8%	$1,053	$1,088	3.3%
WISCONSIN	$13,282	$13,694	3.1%	$5,090	$5,328	4.7%
WYOMING	$5,126	$5,337	4.1%	$76	$80	4.5%

In-Depth Analysis of the Economy

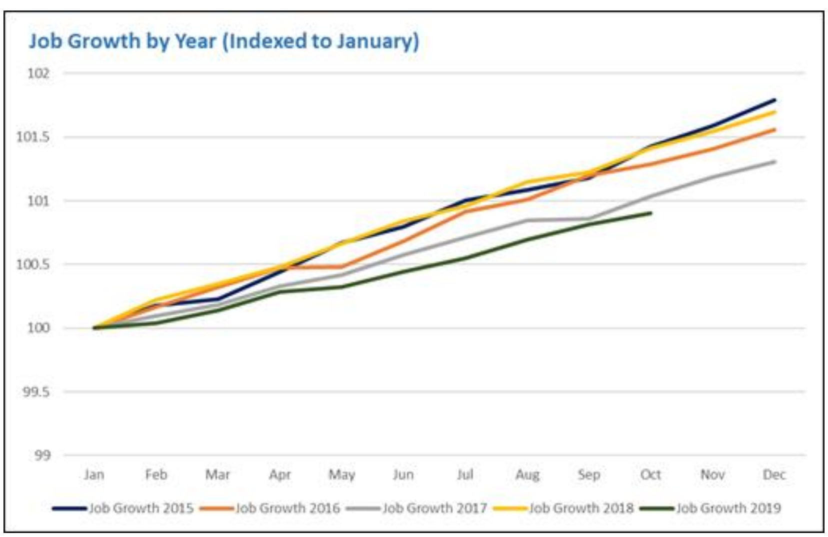
Employment & Wages

Unemployment, payroll and wage growth continue to be a bright spot in the economy and for franchising. Franchise sectors, especially the food and personal service sectors, continued to be supported by the strong employment and wage numbers. The tight labor market is especially impactful on lower-wage jobs filled by younger hires, such as in franchising. In 2020, franchises should expect to see tight competition for an increasing limited labor pool, which will lead to "job hopping" and demands for better wages[14].

FRANdata estimates that over 8.6 million people will work in franchising, an increase of 2.8% over 2019. While this is positive, over the last five years, franchise employment, just like total employment, has been growing at a slower rate.



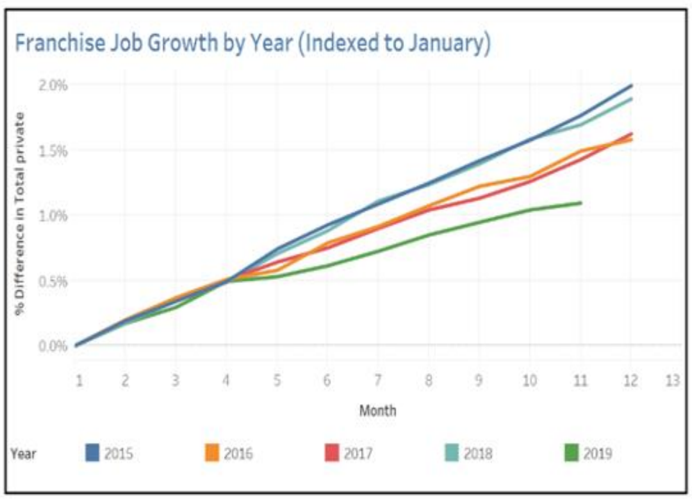
Since 2015, with the exception of 2018, annual job growth has been declining. 2018 was an impressive year of surprising job growth, and 2019 is on pace. Comparing the January to October job growth for 2015 and 2019 shows that 2019 is 0.51% below the pace set in 2015. For 2020, the economy is forecast to add approximately 150,000 jobs per month, which is down from the 170,000 added in 2019 and the 230,000 added in 2018[15].



For October of 2019, the national unemployment rate was at 3.6%, the lowest it has been since the late 1960s, which is believed to be almost as low as unemployment can possibly go. In 2020, unemployment is expected to remain low (approximately 3.7%) as job growth continues, but at a slower pace[16].

This job growth has begun to have a positive impact on wages for the first time in more than a decade. Since Q1 2015, wages and salaries have been improving after being flat for the prior 15 years. This wage growth is expected to continue into 2020 as low unemployment increases demand for employees[17]. And while wages are growing, they have not yet reached the Fed's goal of 3.5 to 4%. Even so, the tight labor market should make that goal obtainable in 2020.

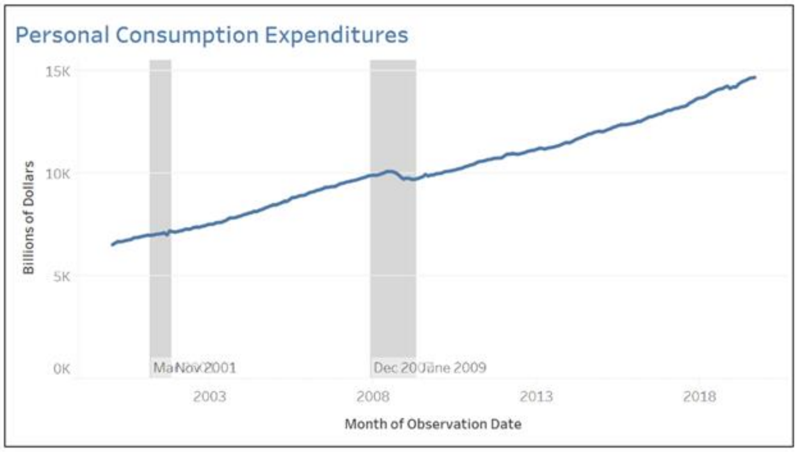
Another factor driving wage growth is increased minimum wage. At the start of 2020, many states are raising their minimum wage to as high as $15 per hour. While the overall impact of this increase is unknown, the results in some of the earliest adopters have been mixed. In some markets, it has shown to be a boon to the poorest people, but has come at the cost of a decreased number of jobs. The general consensus seems to be that while economic inequality is an important issue, increasing minimum wage is an ineffective way to tackle the problem[18].



Consumer Spending and Confidence

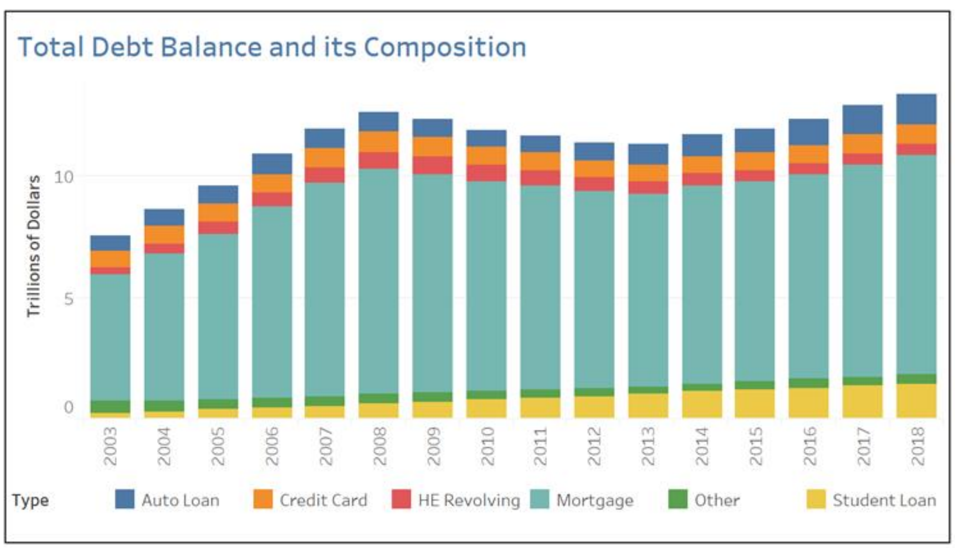
The current recovery has been mostly driven by US consumer spending. Consumer spending accounts for nearly 70% of the total economy[19]. Since the end of the last recession, consumer consumption has been on a continuous upward trend, and unlike job growth, this trend shows no signs of slowing. Improving consumer sentiment and consumer spending are both strong positives for franchising, and as long as these factors remain positive, franchising should be well-positioned for success in 2020.

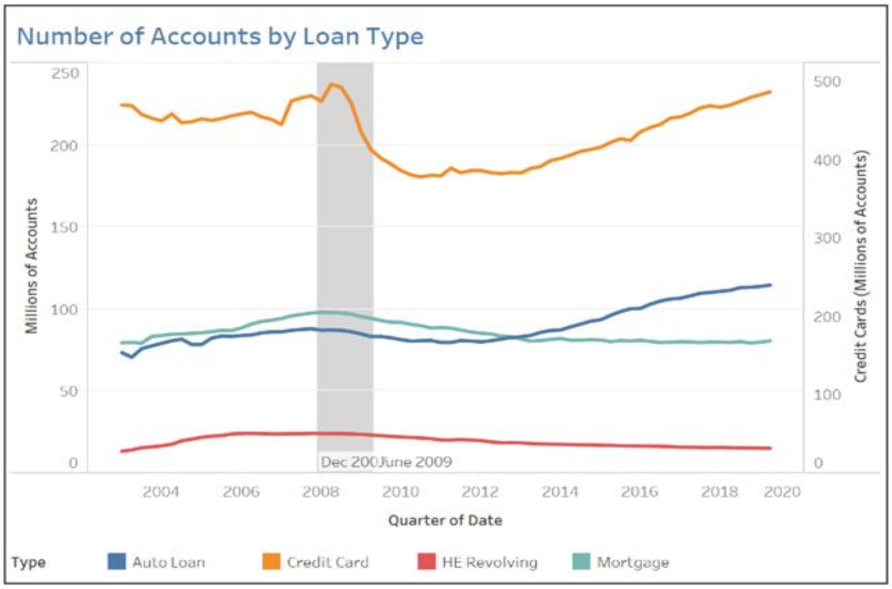
Most forecasts for 2020 expect consumer spending to remain on pace or slow down slightly. The largest threat to continued consumer spending is household debt.



In the first quarter of 2017, US household debt surpassed the high set before the 2008 recession, and it has continued to grow. The majority of US household debt (68%) is held in mortgages. Student loans (11%) make up the next largest portion of household debt. As household debt increases, the amount of income left over for other spending is reduced.

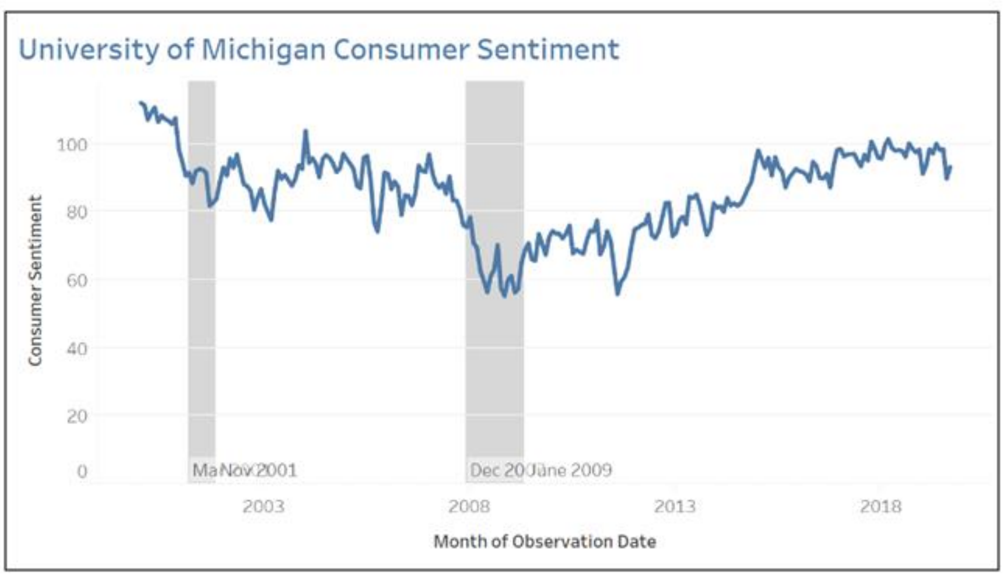
Credit cards and auto loans dominate the new debt added by the amount of new accounts. Since 2010, US consumers have added almost 35 million auto loans and more than 100 million credit cards to their balance sheets. This is an annual growth rate of 3% for auto loans and 2% for credit cards. This consumption has helped drive economic growth, but constantly adding debt will not be maintainable.





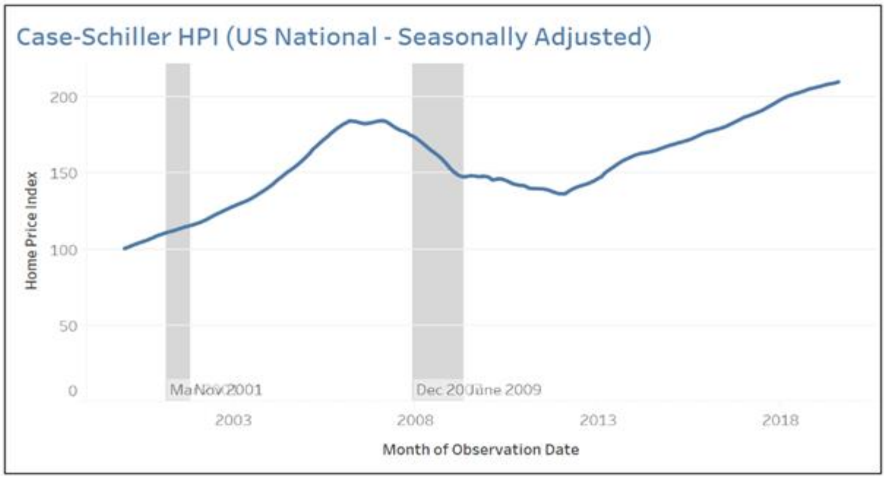
Despite this increase in household debt and added credit card and auto debt, new foreclosures and bankruptcies have been on a downward trend. Consumer bankruptcies are down by an average of 12% per year and foreclosures are down an average of 6% per year[20].

Consumer confidence also continues to improve. In the last two years, consumer confidence has steadily grown at an annual growth rate of 5% in 2019, up from 2.15% in the previous year. Despite an increasing trend, consumer confidence has been volatile, falling from a high of 100 in May to 93 in September. Factors, including the perceived economic slowdown, the trade tensions between the US and China, and slower job growth, have caused consumers to be less optimistic about the short-term outlook. According to a senior director of economic indicators at the Conference Board[21], the strong labor market allows for consumers' remaining confidence; however, the level of confidence will likely decline further if the pattern of uncertainty and economic slowdown persists.

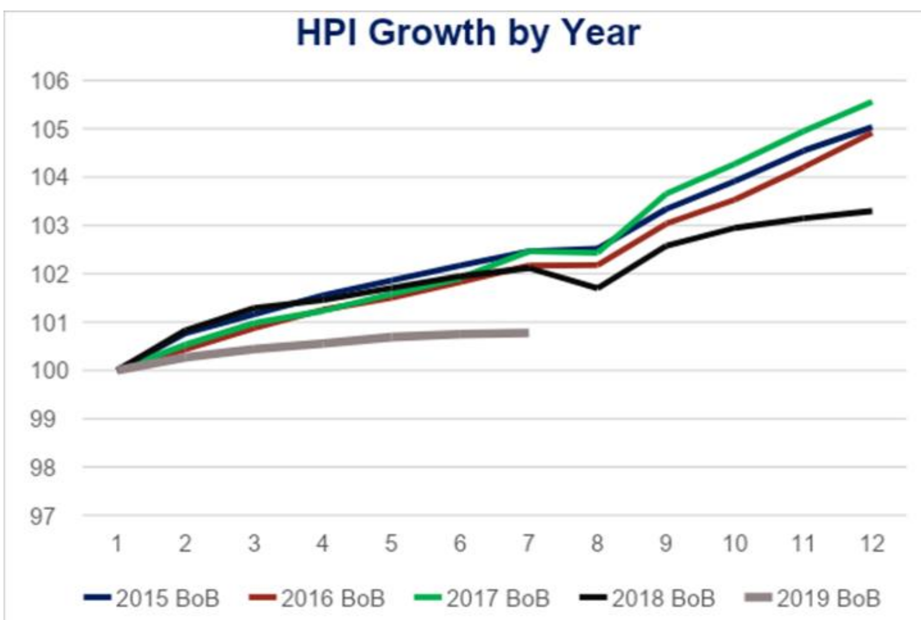


US Housing Market

Since the Great Recession, the US housing market has made a slow but steady recovery. In January of 2018, the Case-Schiller Home Price Index (HPI) had recovered to the previous high of 206.6 that it was in April 2006. Housing is the largest single asset most Americans own. They are dependent on that equity for everything from debt consolidation, to paying college tuition, and retirement. In many ways, the US economy stands on the strength of the US housing market. That makes the long recovery of the last decade extremely important to the overall health of the economy.



Recently, recovery has begun to slow. The 2019 home price growth has been the slowest of the last five years. From 2015 to 2017, HPI grew at more than 5% per year. In 2018, that rate dropped to 3%, and through the first six months of 2019, the growth rate has been less than 1%. At the same point in the previous four years, that growth rate had been above 2%. According to Realtor.com, the slowing home prices highlight the tension between buyers eager to take advantage of lower mortgage rates and potential sellers' concerns about slowing price growth[22].



This trend points to the precipitous drop in the US housing market, which many experts have begun to predict in 2020.

Fannie Mae has been growing consistently more bearish in 2020, having reduced its forecasts for economic growth from 2.1% to 1.5%. It points to softening business investment and weakening economic global conditions[23]. In a recent interview with Robert Schiller, the Noble Prize winner who helped create the Case-Schiller HPI, he pointed to similarities between 2006 and the current market, though he does not expect the next housing bear market to be as severe as the last recession[24].

Housing starts, another important measure of the health of the US housing market, are also improving, but have not reached pre-recession levels. The strong job and wage data combined with low-interest rates likely explain the positive housing starts trend.

The housing market appears to match the general trend of the rest of the economy, a continued but slowing growth.

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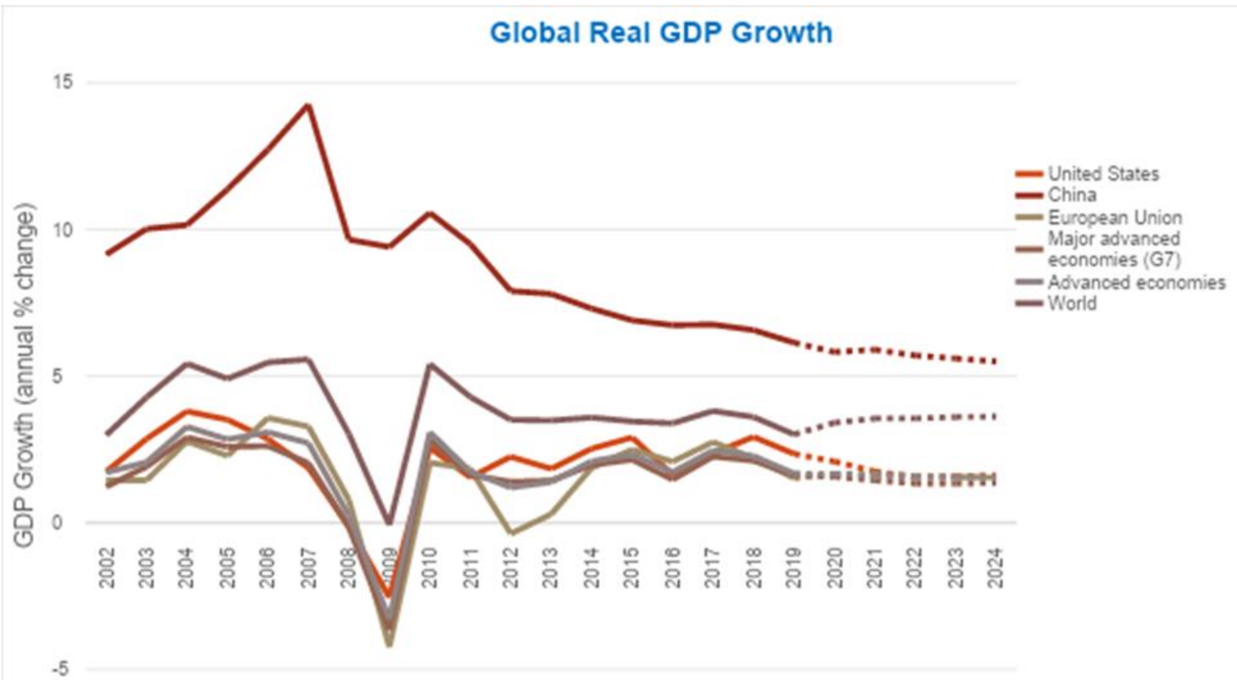
Impact of Global Economy and Trade Policy

The 2008 financial crisis highlighted how interconnected the world economy is. Factors around the globe will have an impact on the US economy and therefore in all franchises. As an example, the trade issues with China has negatively impacted food prices here in the US, tightening already razor-thin margins for restaurants.

According to the IMF, GDP growth will slow down across the globe in the next five years. Countries like the United States, China, and the G7 collective of countries are projected to experience a slowdown in growth followed by a steady 1% percent change each year, while the world aggregate is estimated to slowly increase their GDP growth annual percent change. Global growth is expected to slow to 3% this year, the lowest level since the financial crisis[25]. The IMF explains that this could be a consequence of tariffs and geopolitical tensions around the world that are taking a toll on business confidence, investment, and global trade.



Source: IMF World Economic Outlook (October 2019)

The European Central Bank is taking steps to prevent a downturn by decreasing interest rates; however, it is worried about the limited power it has to stimulate the eurozone economy. European nations will have to increase fiscal policy, given the fact that monetary policy won't be an option due to the already low rates[26]. Currently, the ECB has a negative interest rate, forcing banks to lend more money. Other nations, like Japan, also currently have negative interest rates, which limit their monetary policy ability. Germany, the powerhouse of the European economy, is also expecting a recession soon.

Political uncertainty in major events like the upcoming withdrawal of the United Kingdom from the European Union has raised concerns about the economic impacts it will have. According to the German think tank Bertelsmann Stiftung, the United States could benefit from the possibility of the UK not having a trade deal with the EU[27].

The ongoing trade disputes between the United States and China have increased world economic uncertainty and have raised concerns about the short-term and long-term economic impacts these tariffs could have on the national economy. As of now, there are indications that the situation will deescalate.

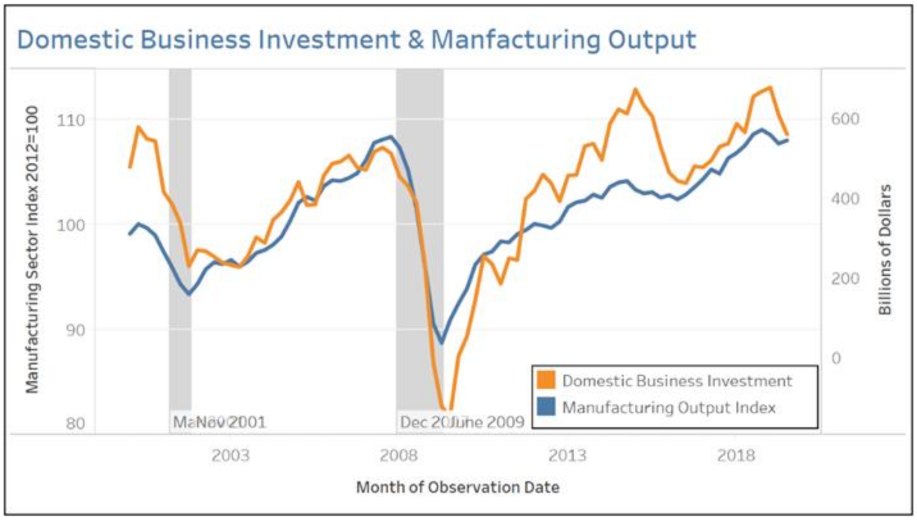
Economic theory, backed by a 2018 report by the NBER, tells us that tariffs imposed by the United States on imports are reducing real income for domestic consumers by increasing the costs of goods sold. These tariffs directly impact the supply chain of many franchises in the United States, forcing them to either find cheaper alternatives or use more expensive inputs than without the tariffs[28]. The size of the impact will depend on the sector in question. These new policies might benefit the franchise food industry in the short term due to the inability of domestic farmers to export to China, leaving them with a surplus that could only be sold by a decrease in price driven by a government subsidy. Nonetheless, if the trade dispute continues, domestic prices will increase in the long-run, forcing restaurants to modify their supply chains.

GDP growth was reduced from previous forecasts as a consequence of these tariffs. According to a report done by IHS Markit, global GDP was reduced by 0.1% in 2018 and will be reduced by 0.8% in 2019 and 1.4% in 2020[29]. Concerning the domestic economy, Goldman Sachs calculates that the trade war has already cost 0.6% of the GDP[30]. Similarly, the Peterson Institute for International Economics believes that the ongoing disputes “contributed to the decline in business fixed investment, and [are] likely subtracting about half a percentage point from growth in gross domestic product this year[31].”

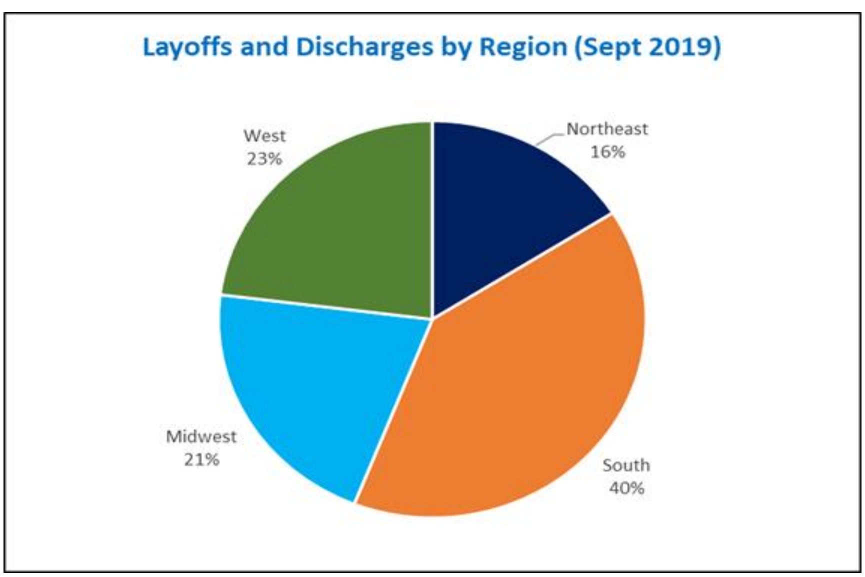
Besides added uncertainty, tariffs also adversely impact input prices and raise costs along the supply chain, all of which can negatively impact franchising, especially in the retail space. The tariffs have also negatively impacted food prices as farmers have had to raise prices to offset decreased international demand for their goods[32]. It is possible the trade disputes, especially with China, will deescalate soon, but there is a great deal of uncertainty around that.

Business Investment and Outlook

As 2019 finishes and planning begins for 2020, there are clear signs that the longest economic expansion in history is coming to an end. In no part of the economy is that clearer than in business investment. Since a peak in January of 2019, net domestic business investment has fallen 17%. At the same time, manufacturing output had also dropped, with a slight improvement from Q2 to Q3 2019. The general consensus is that business investment has been adversely affected by the uncertainty created by the trade disputes[33].



Business fixed investment has been contracting in the past few quarters with a negative growth rate of -0.94% in the third quarter, a drop from a 3.0% gain in the first quarter of 2019. Despite a cut in the interest rate coupled with a reduced tax rate on corporate profits, many business owners are reluctant to purchase equipment to rebuild the supply chains. The contraction is dramatic in the U.S. manufacturing sector, as a consequence of the ongoing trade war. The imposition of tariffs on international goods increases production costs, leading to business owners holding back the investment plans until a trade deal is made.

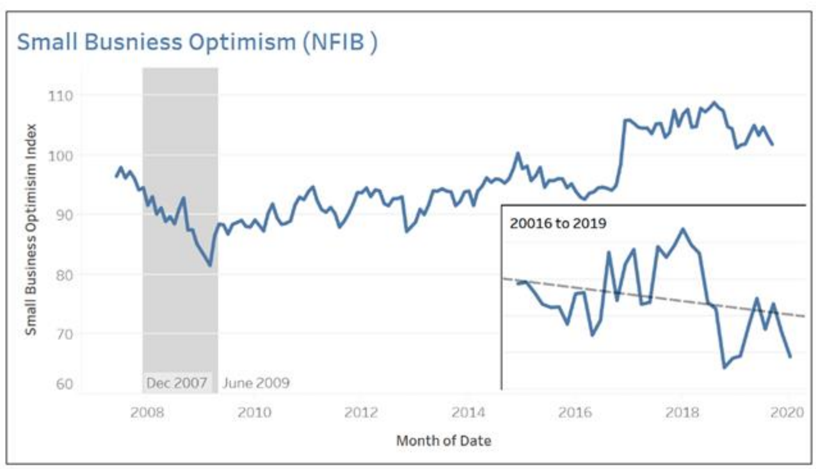


At the same time, manufacturing output is also declining. A slowdown in manufacturing could create drag on related industries and disproportionately affect parts of the country least able to absorb those displaced employees[34]. From July to September, the Bureau of Labor Statistics reports that manufacturing and mining laid off approximately 366,000 employees, a 4% increase over the previous three-month period[35]. These layoffs and discharges were most concentrated in the South, followed by the West, and then the Midwest[36].

There are signs that these issues will continue into 2020. The Institute for Supply Management (IMS) reports that new orders, production, employment, and raw material inventories are all contracting. The order, production, and employment rates have been trending downward for three months and the inventories trend has been consistent for five months. Across the board, the IMS reports the entire manufacturing sector has been contracting for the last three months[37].

The Organization for Economic Co-Operation and Development (OECD) survey of US manufacturing is even less optimistic. The OECD's index of their manufacturing survey has been declining since August 2018, and the last time the index was this low was May of 2009, which was right at the end of the recession.

This negative view of manufacturing is a useful indicator of economic health, but manufacturing isn't a small business. The National Federation of Independent Business' (NFIB) small business confidence index also shows a decline.



NFIB's small business confidence is up from the last recession, but as the inset table shows, the trend has been negative since December 2016. The September 2019 number is 4% below the December 2016 number and also 6% below the peak of August 2018. The declining small business optimism harms fixed business investment, as small business owners have a less optimistic outlook for business and sales. According to the NFIB President and CEO, owners' willingness to invest is mostly affected by the economic uncertainty and a lack of qualified workers[38]. The business fixed investment is expected to grow at a slower rate of 1.3% in 2020, according to Deloitte's economic forecast.

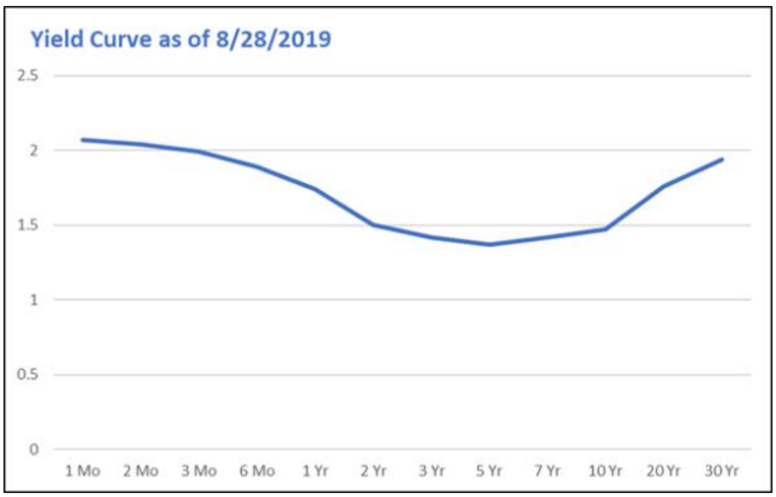
This general decline in manufacturing and small business optimism both point to potential headwinds and more uncertainty for franchising. While most franchise brands are service-based, loss of regional manufacturing jobs can't dramatically impact franchise brand performance. The decline in small business optimism highlights the impact of economic uncertainty that has been swirling around the economy within the last year, which is expected to continue or worsen.

FRANdata

Interest Rates & Small Business Lending

As the last recession taught us, capital is the oil that keeps the engine of the economy running smoothly. Any disruption in the flow of capital can have ripple effects throughout the economy. Based on interviews performed with franchise lenders, FRANdata believes that lender expectations are slightly negative. The two most common concerns mentioned were a general recession and an increase in the number of less qualified borrowers. Just over 20% of those interviewed mentioned that they've seen a slight decline in application quality in the last six months and 30% expect to see application quality continue to decline in the new year. One lender summed this up best when they said, "It looks like a lot of franchisors are having to dig deeper into their pipeline of potential franchisees to meet goals, and that has led to a decrease in the quality."[39]

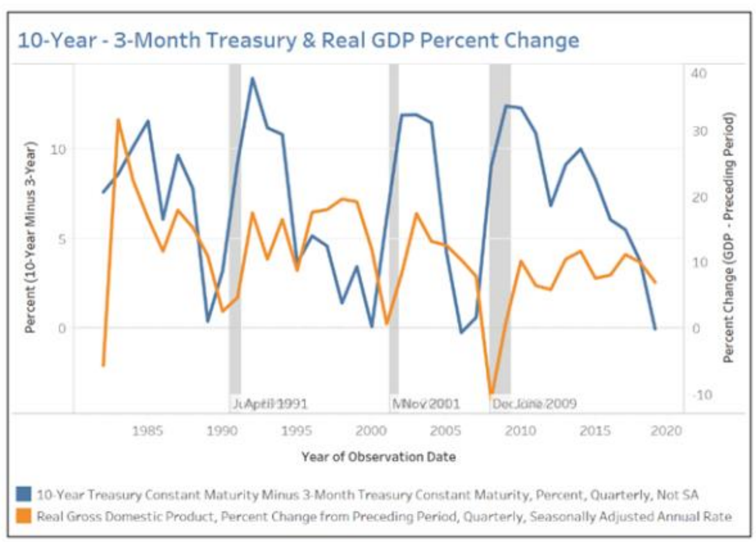
To be clear, the economy is an exceptionally complex system, and there are positives and negatives to be found everywhere. The single-most concerning warning light for the economy is the inverted yield curve. From August 27th to September 4th, the three-month maturity T-bill had a higher return than the 10-year, which means investors are so worried about the future that they are willing to pay a premium for short-term maturities.



The inverted yield curve has been an accurate predictor of recessions every time it has happened. The timing is less consistent but ranges from two to eight quarters afterward. That means a recession may happen anywhere in 2020 or early 2021.

The following table shows the last three recessions, and in all three cases, a recession occurred within four quarters of the inversion. Assuming this trend continues, a recession could begin as soon as late summer of 2020.

These concerns about the yield curve and interest rates have yet to trickle into the lending environment. Currently, all forecasts for small business lending appear positive, especially from the SBA.



Bank lending is not the only source of capital for franchisees. Alternative sources of financing and FinTech options are growing and might provide relief if banks begin to tighten credit requirements.

The alternative lenders have been growing and attracting attention, particularly from small and medium businesses (SMBs). It is driven by the rise of the start-up businesses (emerging brands) and an increase in alternative lending options such as lines of credit and invoice factoring. On the other hand, according to the Wall Street Journal report, big banks have reduced the volume of loans to small businesses by more than 36% since 2016. The bank-loan success rate has also decreased. As a result, the small business finds it harder to secure bank loans from traditional lenders. Compared to traditional banks, alternative lenders are usually based online, have low loan qualification requirements and quick funding at the expense of paying high interest rates. Therefore, the presence of alternative lending is likely to fill the gap between the financing needs of SMBs and traditional bank financing.

According to a report by S&P Global Market Intelligence, annual loan originations by an SMB-focused platform was $7.89 billion in 2018 with a CAGR of 21.2%. It is estimated that SME-focused lenders will originate $10.77 billion in new loans in 2020, where the loans are projected to grow at a slowing pace, with an estimated CAGR of 16.1%.

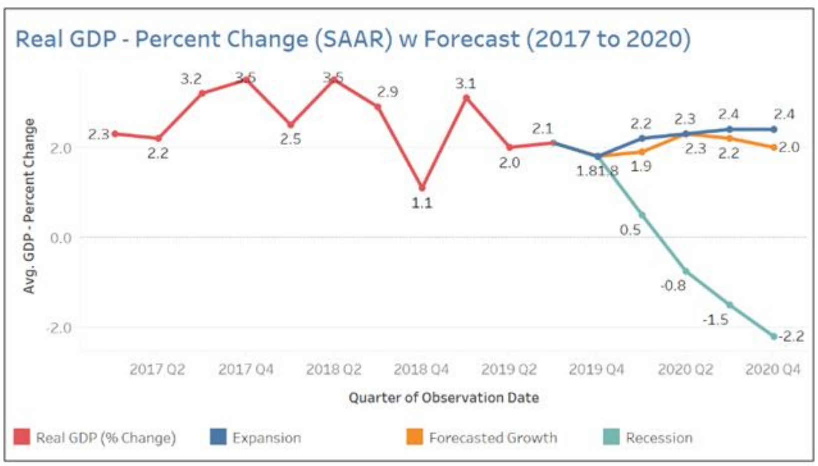
Expectation for GDP and Franchising in 2020

The long recovery that started in 2009 is coming to an end, but FRANdata expects the economy to have enough forward momentum to stave off a recession until 2021. Instead, we expect the economy to continue to expand, but at a slower pace than 2019.

Scenario	Likelihood	2019 Q1	2019 Q2	2019 Q3	2019 Q4*	2020 Q1*	2020 Q2*	2020 Q3*	2020 Q4*	2020*
Real GDP (% Change)		3.1	2.0	2.1	1.8					
Forecast	70%					1.9	2.3	2.2	2.0	2.1
Recession	25%					0.5	-0.8	-1.5	-2.2	-1.0
Expansion	5%					2.2	2.3	2.4	2.4	2.3

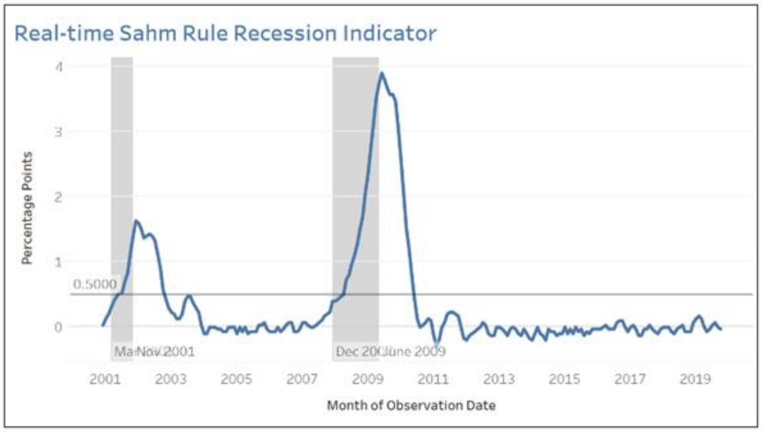
*Forecasted Data

Based on an aggregation of available forecasts, FRANdata expects a Q4 2019 GDP growth of approximately 1.8%, which gives 2019 a total GDP growth rate of 2.3%. In 2020, FRANdata expects that growth rate to continue to decelerate to 2.1% for the year. We believe there is a 25% chance of a recession in 2020, which would drop GDP growth into the negative by Q2 and leave 2020 with a negative growth for the year. We also feel that there is a 5% chance of expansion in 2020. If there was a resolution in trade policies and global economic issues such as Brexit, it is possible, but unlikely, 2020 could outperform 2019.



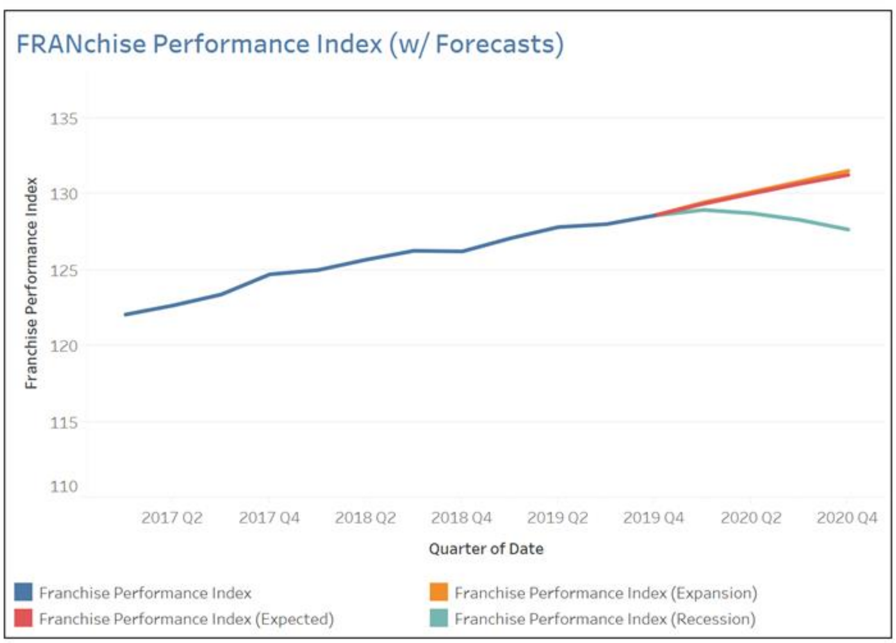
As the year progresses, FRANdata recommends watching the Sahm Rule Recession Indicator, as it appears to be an excellent measure of identifying when a recession has begun.

The Sahm Rule, created by Claudia Sahm of the Federal Reserve, measures the average three-month unemployment rate. When that rate crosses the .5% line, a recession has begun. This would provide up to six months of advance notice on the traditional identifier of two quarters of negative GDP growth. Currently, the Sahm Rule sits just below zero, but is worth keeping an eye on, as it appears to be the earliest possible indicator of a recession beginning.



Based on FRANdata's analysis of franchising and its relationship to the rest of the economy, we believe that an annual GDP growth rate of 2.1% would translate to a 1.8% growth rate for the Franchise Performance Index. In the 25% chance of the recession, we'd expect to see the FPI to contract by -.9%, and in the expansion model, the FPI would grow to 2.1%.

Assuming other relationships remain constant, FRANdata forecasts franchising will add over 8,000 units in 2020, reaching a total of approximately 785,316, with total employment at 8,666,141 and total economic output at $819.6 billion.



Methodology

FRANdata calculated franchise establishments, employment, and output per business line for 2016-2018 using our internal database, Fratsweb, the largest database of franchise information in the nation, with more than 40,000 franchise documents going back 30 years, as well as combining information gathered from the U.S. Census Bureau. In this year's report, the historical franchise business performance was also informed by the past research in order to keep trend consistent, and we have arranged the entire franchise industry into eight business lines instead of 10 from the previous Franchise Business Economic Outlook Report by merging the Automotive sector and the Retail Food sector into a combined Retail Food, Products & Services sector. We estimated the 2019 franchising activity and projected the 2020 franchise industry growth by building the econometric forecast model as well as using the FRANchise Performance Index created by FRANdata. The model factored in the historical franchise business growth performance and macroeconomic indicators such as the unemployment rate and the GDP growth rate.

For state level franchising activity, we calculated each state's franchise establishments, employment, and output for 2016-2018 based on the information from both Fratsweb and the Census Bureau, and estimated each state's contributions to the franchise industry as a whole for 2019 and forecasted for 2020. We then multiplied each state's proportions to the franchise industry's total establishments, employment, and output in order to estimate the state level franchise business economic impact for 2019 and 2020.

Appendix

1. **Business Services:** Includes printing, business transportation, warehousing and storage, data-processing services, market research and business consulting, advertising and public relation, commercial banking, insurance agencies and brokerages, office administrative services, employment services, legal, investigation and security services, tax-preparation and payroll services, and heavy equipment leasing.
2. **Commercial & Residential Services:** Includes building, developing, and general contracting; heavy construction; stone product manufacturing and special trade contractors; facilities support services; services to buildings and dwellings; and waste management and remediation services.
3. **Lodging:** Includes hotels, motels, and other accommodations.
4. **Personal Services:** Includes educational services, fitness centers and healthcare, entertainment and recreation, hair care, tanning salons, cosmetic aids and services, massage and spa, laundry and other personal care services, veterinary services, loan brokers, credit intermediation and related activities, and personal transportation.
5. **Quick Service Restaurants:** Includes limited-service eating places, cafeterias, fast-food restaurants, beverage bars, ice cream parlors, pizza-delivery establishments, carryout sandwich shops, and carryout service shops with on-premises baking of donuts, cookies, and bagels.
6. **Real Estate:** Includes lessors of buildings, mini warehouses and self-storage units, and other real estate property; real estate agents and brokers; and property management and other related activities.
7. **Retail Food, Products & Services:** Includes food and beverage stores; convenience stores; food-service contractors; caterers; retail bakeries; beer, wine, and liquor stores; gas stations with convenience stores; motor-vehicle parts and supply stores, including tire dealers, automotive equipment rental and leasing, and automotive repair and maintenance; furniture and home furnishings stores; electronics and appliance stores; building material and garden equipment and supplies dealers; health supplement, pharmacies and drug stores; beauty supplies and optical goods stores; clothing and general merchandise stores; office supplies and stationery stores; florists and gift stores; used merchandise stores; consumer-goods rentals; photographic services; and book and music stores.
8. **Table/Full-Service Restaurants:** Establishments primarily engaged in providing food services to patrons who order and are served while seated (i.e., waiter/waitress services) and pay after eating.

End Notes

1. “US Economy Grew at a Moderate 2.1% Annual Rate in the Third Quarter.” CNBC, 27 Nov. 2019.

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End Notes

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About FRANdata

FRANdata is a franchise-focused research and advisory company. An industry leader in the strategic analysis, forecasting and measuring of franchise performance. FRANdata harnesses insight and research into analytical and actionable solutions that transform acceptable outcomes into highly successful businesses for our clients. FRANdata is headquartered in Arlington, Va., and is often cited as franchise experts in media publications such as The New York Times, The Wall Street Journal, Forbes Magazine, the Franchise Times, and Nation's Restaurant News. For more information go to www.frandata.com.