Decision and Restaurant Analysis of Boston Pizza and Pita Pit

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Note: All currency amounts are in US Dollars

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Executive Summary

The following content will first examine the comparable differences and similarities between Boston Pizza and Pita Pit. It will compare and contrast both franchising systems on financial criteria and operational requirements. It is evident that Pita Pit is a better system to invest in for the Hamilton area. After analyzing the leading marketing segments consisting of "Millennial, Gen X" within the Hamilton area, it is clear that fast-casual restaurants are an appealing consumer choice for this emerging segment that dominates the restaurant industry. Based on financial projections it is possible to generate a positive revenue stream if it is near pedestrian friendly area such as malls, universities, colleges and suburban shopping districts. The initial investment is substantially lower with the Pita Pit system, lowering the barrier to entry as well as the financial risk. Pita Pit is also better suited for entrepreneurs who do not have previous experience operating a full-scale restaurant through their training program and 24/7 assistance and few employees.

S.M.A.R.T. Objectives

The goals and objectives will be weighed out of ten (10), with one (1) being deemed not at all important, five (5) being sufficiently important, and ten (10) being considered crucial and critically important in the decision process.

<u>Financial Goals</u>

I. The expected initial investment should not exceed $500,000 to open a single unit as a newly admitted franchisee within one calendar year after signing the agreement. If the franchisee is leasing a space, first and last month's rent and a security deposit must be part of the initial investment alongside construction costs. The same conditions apply for buying or building a unit from scratch: the initial investment includes any necessary construction costs, equipment purchases, leasing or buying a storefront, and transfer or negotiation fees. *Weight of Importance: 10*

<u>Operational Goals</u>

I. A minimum of a five-year licensing operation agreement must be offered by franchisor with the chance to renew the licensing deal for another five years. The renewal has to be negotiated, agreeded upon and signed 12 months before the initial contract expires. If there is no chance to renewal the agreement either decided upon by the franchisee or the franchisor, the party who decided not to pursuit a renewal must inform the other 18 months before the initial contract expires. The initiator must present a plan on how to disolve all assets and liabilities in relationship to the business 12 months before the agreement expires to the other party, with a three-month period to review and agree to it. *Weight of Importance: 8*

II. The franchisee can purchase one to two new units when renewing the licensing agreement at a 10% lesser rate of the initial agreement or is permitted to make an investment purchase in other franchise units within the parent company within the same georgraphical area without infriging on the franchisee's original purchase. *Weight of Importance: 4*

Franchise Analysis

Each objective is weighed against the two franchise systems on whether they meet the objectives or not, with an average being calculated at the end in the Decision section. Each system under the analysis can receive partial (i.e. 50%) or full points based on the SMART criteria.

Franchise Analysis: Boston's Pizza

Financial Goals 5/10 points: The prospective franchisee can expect to pay an upfront cost of $65,000 to the parent company (i.e. $50,000 signing fee, $5,000 opening fee and $10,000 pre-opening marketing fee) in addition to the construction and renovation costs of opening a restaurant. There are three types of Franchise Agreements, which include upfront costs paid to the parent company as well as a range of construction and renovation cost options:

I. A single restaurant built from the ground up: $2,019,000 to $3,017,000 (excluding land costs).

II. A retrofitted or shell build-out of an existing structure: $1,145,000 to $2,205,500 (excluding leasing costs).

III. A development agreement in accordance of first two options with an additional payment of $50,000 for every unit to be developed within a specific timeframe (e.g., 3 development units x $50,000 + $15,000 in opening and marking fees).

Operational Goals 10/12 points: The agreement is a ten-year term contract under the Boston Pizza trademark from the date the agreement is signed, including time for construction and operational set up of the franchise unit. There is an option of two renewals with the same contractual obligations for a five-year term each, which must be given in writing to Boston Pizza no sooner than nine months and no later than 12 months from the initial contract termination date. All contract renewals are conditional until Boston Pizza confirms that the franchisee has met the parent company's conditions and has paid Boston Pizza a renewal fee in an amount equal to 50% of the then-current initial franchise fee (i.e. $25,000 in renewal fees). If Boston Pizza or the franchisee does not want to renew the agreement, the franchisee must relinquish all intangible and tangible materials to Boston Pizza. This also includes any passwords and other information used to operate the business. All this must be returned to Boston Pizza within five business days after the expiration date of the agreement and the franchisee must immediately stop operating the business on the expiration date, and pay any outstanding fees to Boston Pizza, and any suppliers and or partners.

Franchisees can only purchase additional new units under a development agreement as discussed previously. Boston Pizza prohibits franchisees to purchase competing restaurants or partake in any franchises outside of the parent company that operate within the casual restaurant industry (Boston Pizza gives a comprehensive list). If the franchisee does not wish to renew their agreement after the ten-year operational period, the franchisee cannot directly or indirectly have involvement with a competing business for two years within a 10-mile radius of any Boston Pizza restaurant, which will be listed by the parent company. If the franchisee violates their agreement (depending on how long the restaurant is open), he or she must pay fines to cover the average amount of royalty fees and advertising funds Boston Pizza would have collected for 36 months or the number of months remaining in the term of the Franchise Agreement upfront.

Franchise Analysis: Pita Pit

Financial Goals 10/10 points: The prospective franchisee can expect to pay an upfront initial fee of $30,000 to the parent company. The Franchise Agreement requires that a lease for a location must be obtained within 12 months after signing and the unit must become open to the public between 60 to 120 days after the lease is signed. If not, the agreement becomes null and void. Franchisees can sign a single unit Franchise Agreement, or can choose a Multi-Unit Development Agreement. Both estimating the cost of construction and renovation, and leasing the necessary space required for operations:

I. A single restaurant costs: $216,354 to $435,102.50 (including the initial fee)

II. A multi-unit development agreement: $216,354 to $435,102.50 per unit + the initial fee of $30, 000 for the first unit + development fee for each additional unit

Minimum Development Obligation	Cost Basis per Restaurant	Development Fee
3 Restaurants	$22,000 per Restaurant	$66,000
4 Restaurants	$20,000 per Restaurant	$80,000
5 Restaurants	$18,000 per Restaurant	$90,000
6 Restaurants	$16,000 per Restaurant	$96,000
7 Restaurants	$14,000 per Restaurant	$98,000

<u>Operational Goals 12/ 12 points:</u> The agreement is a ten-year term contract under the Pita Pit trademark from the date the unit has become open to the public. It excludes any time that it took to find a location, negotiations between the franchisee and the landlord, and the construction and operational set up time of the franchise unit. The franchisee can receive renewal with the same contractual obligations for another ten-year term with a cost of $25,000 plus applicable taxes only if they receive score a 90% or higher on their in-store and system evaluation test, as conducted by the parent company. The franchisee must express their interest for contractual renewal no later then six months before their initial agreement expires. If the franchise scores a 89% or lower on their evaluation or the franchisee does not want to renew the agreement, the franchisee must relinquish all intangible and tangible materials to Pita Pit. This also includes any passwords and other information used to operate the unit within ten business days after the expiration date of the agreement and the franchisee must immediately stop operating the business on the expiration date, and pay any outstanding fees to Pita Pit, and any suppliers and or partners.

Franchisees can only purchange additional new units under a multi-unit development agreement as discussed previously. Pita Pit prohibits franchisees from purchasing competing restaurants or partaking in any franchises outside of the parent company regardless of the restaurant segment it operates in. If the franchisee does not wish to renew their agreement after the ten-year operational period or if the contract is terminated by the franchisor, the franchisee cannot directly or indirectly have involvement with a competing business for two years within a 5-mile radius of the franchisee's previously operated unit. If the franchisee violates these terms of agreement, the parent company is permitted to seek legal action without warning against the violator.

Decision: I have chosen the fast-casual restuarent Pita Pit because it presents a better financial opportunity for a first time franchisee based on the initial investment required. It allows prospective franchisees to find a suitable location within a generous amount of time and presents less restrictive and costly measures to build a unit and conduct operations. The restaurant meets the crucial criteria of the financial objectives compared to Boston's Pizza and presents an easy renewal process within the evaluation criteria, with a possibility of operating the business for 20 years in totoal.

	Criterion	Weight	Pita Pit	Boston Pizza
Financial Criteria	Franchise should not exceed $500,000 total investment	10	10	5
Operational Criteria	Minimum five-year licensing operation agreemen with the chance to renew the licensing	4	4	4
	Termination Plan	4	4	4
	The possibility of purchasing other franchise units	4	4	2
	Total Point Possible	22	22	15

Market Analysis

Market Trends and Feasibility Analysis: Consumers are becoming more aware of their health and are taking a proactive approach towards bettering themselves by engaging in preemptive measures to ensure a healthy lifestyle, especially amongst youth (Gustafson, 2017, para. 1). Canadians are no longer relying on quick diets and weight loss fixes to remain fit and healthy; rather, 44% of Canadians are taking an active role in monitoring their food intake because they either want to: improve their health, lose weight or prevent any future possible health issues (refer to Figure 1-2). Due to this factor, many consumers are turning away from fast-food restaurants like McDonald's and are choosing fast-casual restaurants such as Freshii and Pita Pit for their alternative, healthy and quick service options. Consumers are no longer satisfied with the subpar veggie burgers offered at traditional mainstream restaurants and want to take control over their meals. They are looking for a variety of vegetarian, vegan or alternative protein meals in the restaurent industry and unfortuntately major players "are the latest link of the food chain taking notice that more consumers are turning to alternative protein because of high meat prices, as well as environmental, humanitarian and health reasons" (Sagan, 2018, para. 2). Furthermore, according to RestoBiz (2018), one of the biggest trends across the restaurant industry is "build your own" since consumers want to customize their menu options to their unique tastes and preferences, without inconveniencing the food preparation staff by asking to remove certain components of the meal. As such, this has presented an entry point for new and emerging competitors to enter a niche market in the fast-casual restaurant industry by offering healthy meals with quick and friendly service traditionally found in the quick-service industry.

Competitive Analysis: Currently, there are five Pita Pits operating in five distinct Hamilton neighbourhoods: Westdale Village (near McMaster University), downtown Hamilton (Jackson Square Mall), two in the East End (one in The Centre Mall and another one walking distance from it) and Upper James Street (the major restaurant segment of the city). Also, Hamilton's population sees an increase of students moving into the city to attend Mohawk College on the mountain and McMaster University, which is within walking distance from the downtown core. Currently, the city presents a significiant opportunity for eager franchisees to began operations since the rent and restaurant construction prices present a cheaper and simplier option to begin operations compared to other neighbouring cities such as Burlington, Oakville and Toronto (Sponagle, 2018, para. 16-17).

Target Customer and Segment Analysis: Since this emerging trend is significantly present amongst young people, I feel that the best demograpic for Pita Pit to target would be millinneials and gen Z, those aged between 15 – 35 years old, in Hamilton, Ontario, Canada. According to the 2010 Census, 19% of Hamilton residents are aged between 15 to 29 years, and another 19% are between the ages of 30 to 44 (refer to Figure 3), representing a large market share of young hungry consumers.

Operating Analysis

Local Promotional Plan: I plan to work with Hamilton sports teams through sponsorships. Pita Pit can easily participate in the monthly Art Crawl, a local art festival, through catering sample events, distributing filers alongside ready made wraps. However, the best promotional plan would be to locate the franchise unit near a school (i.e. secondary or post-secondary school) and offer student discounts to increase foot traffic and interest in the area.

Location and Timing Exection: A potential option to open a franchise location would be near Mohawk College, because of the continuous flow of students during the school year and alternative students and camp attendees during the summer months. The area that surrounds Mohawk College lacks any quick-service restaurants, as students' only food option would be their on-campus cafeteria and residents have to travel downtown to reach any restaurant or travel to Uppper James Street. The other location option would be the Meadowlands situated in Ancaster, a subburb of Hamilton. The Meadowland area consists of many casual restaurants, an open plaza centre and the residents of the area consist of young familties. Pita Pit would have to compete amongst region favourites like Kelsey's and other quick-service chains such as Quiznos. The last potential area would be Lime Ridge Mall food court. Lime Ridge Mall is the biggest indoor shopping mall in Hamilton and sees many customers daily. It is the only one of the three malls in Hamilton that does not have a Pita Pit location; however, acquiring a store unit is competitive in terms of price and such an opportunity does not come about too often. Thus, Mohawk College represents the best possible location because of the lack of nearby competition and high rate of student customers.

Financial Analysis

I forecasted the first year's sales at $400,000 as a conservative estimate based on the average sales of other Pita Pit locations. Some Pita Pit locations have sales in excess of $1,000,000 while others are less than $200,000. I feel that based on the location and demographic of the area, sales of over $400,000 are achievable as well as a modest increase of 15% in the second year and 10% in the third year.

Revenue	**Year 1**	**Year 2**	**Year 3**
Sales	$400 000	$460 000	$506 000
Amortization	$30 000	$30 000	$30 000
Royalties (5%)	$20 000	$23 000	$25 300
Advertising Fees (1%)	$4 000	$4 600	$5 060
Gross Revenue	$346 000	$402 400	$445 640
Expenses			
Food and Beverages (Estimate of 35% of Sales)	$140 000	$161 000	$177 100

Payroll Expenses and Taxes (Estimate of 25% of sales)	$100 000	$115 000	$126 500
Repairs and Maintenance	$8 000	$8 200	$8 400
Rent	$36 000	$38 000	$40 000
TMI	$8 400	$8 600	$8 800
Utilities	$15 000	$16 000	$17 000
Insurance	$2 000	$2 100	$2 200
Miscellaneous Cost	$12 000	$12 000	$12 000
Profit (Loss)	$24 600	$41 500	$53 640

Cash Flow	**Year 1**	**Year 2**	**Year 3**
Operating			
Cash Receipt	$400 000	$460 000	$506 000
Amortization	$30 000	$30 000	$30 000
Cash Paid to Franchisor	$24 000	$27 600	$30 360
Cash Paid to Suppliers and Employees	$321 400	$360 900	$392 000
Net Cash Provided by Operating Activities	$24 600	$41 500	$53 640
Investing			
Cash Payment for Lease Hold Improvement	($145 000)		
Downpayment on Equipment Purchase	($25 000)		

Net Cash Used in Investing	($170 000)		
Cash Net Change	($145 400)		
Cash Beginning Balance	$300 000	$154 600	$196 100
Cash Ending Balance	$154 600	$196 100	$249 740

Exhibits

Figure 1

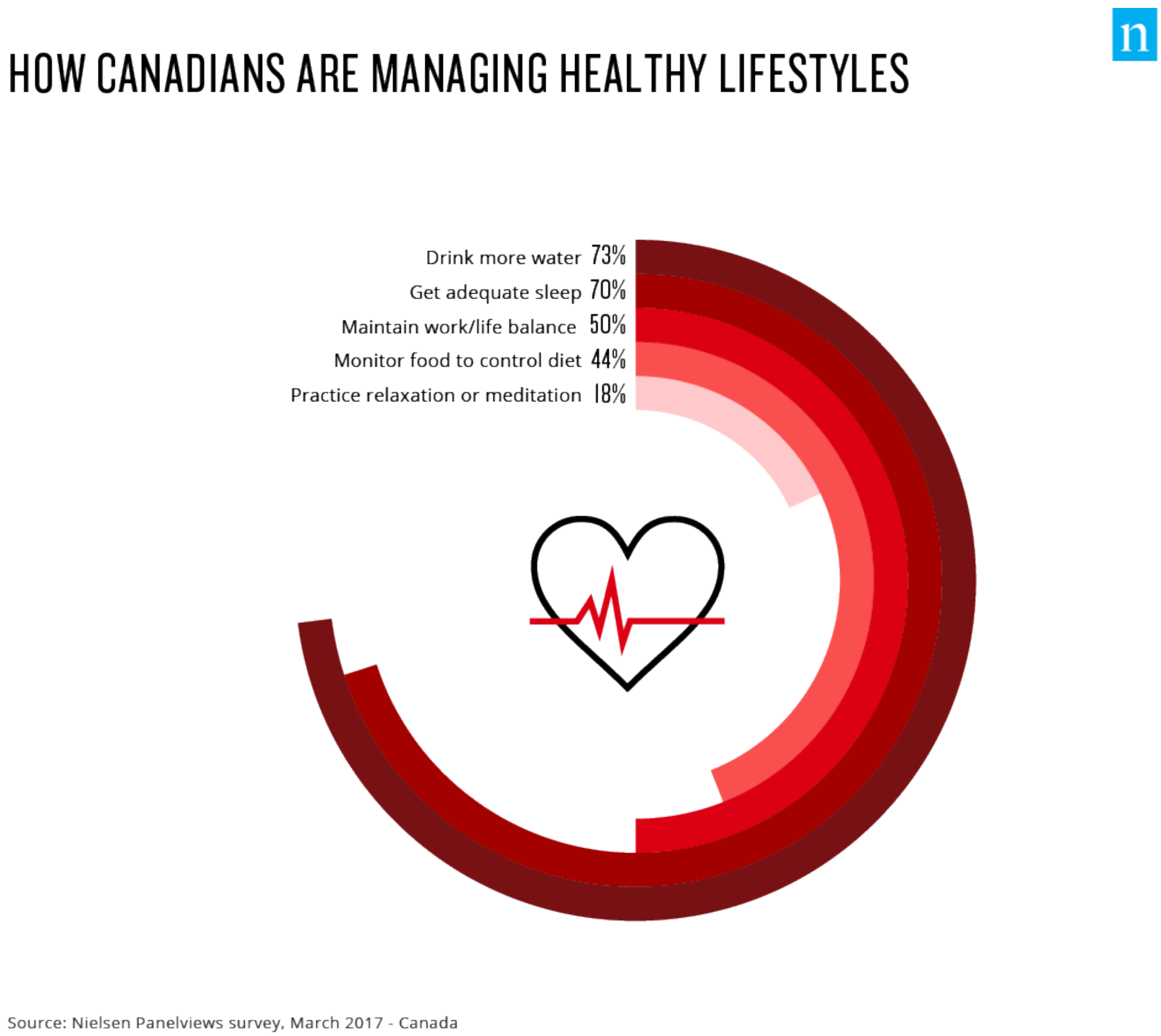


Figure 2

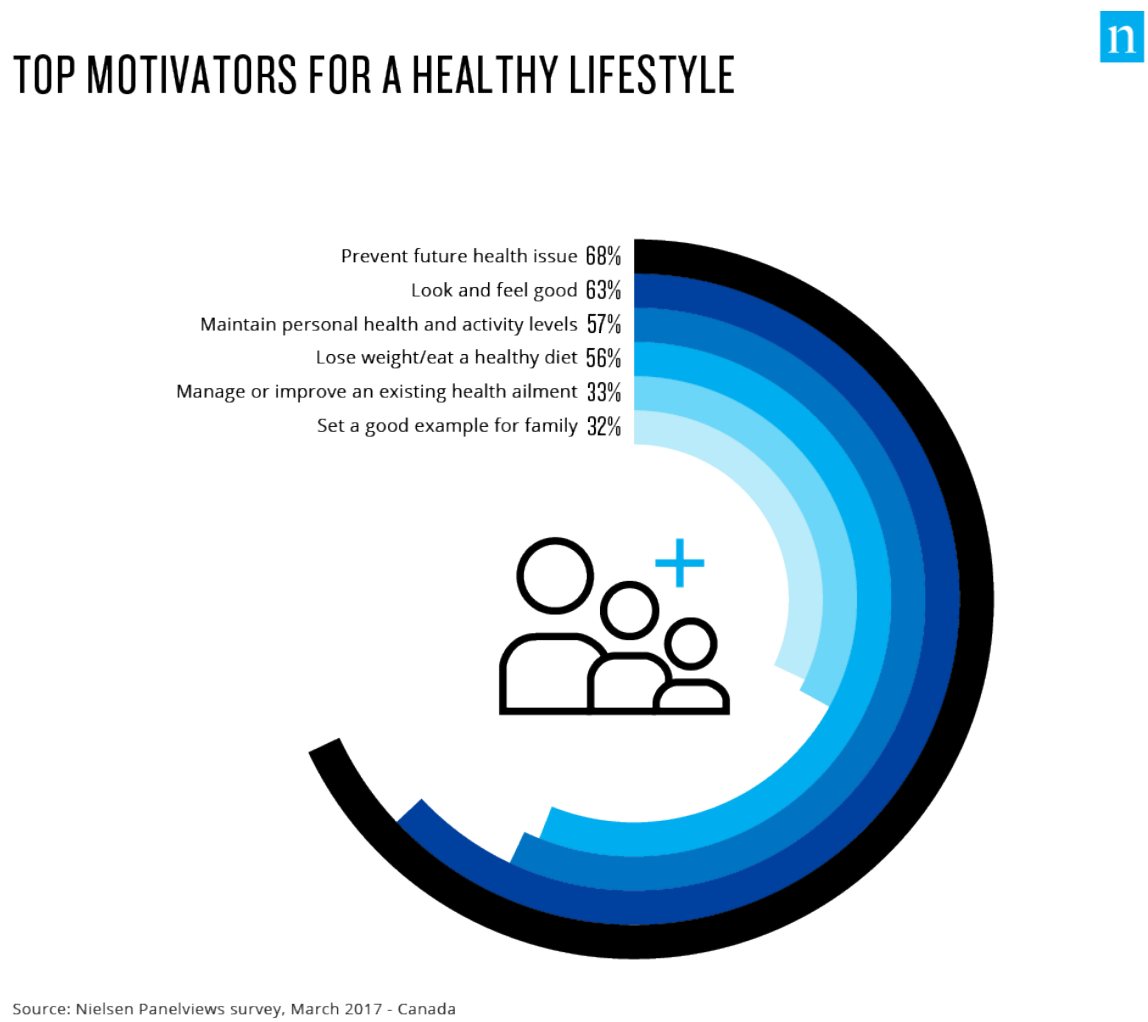
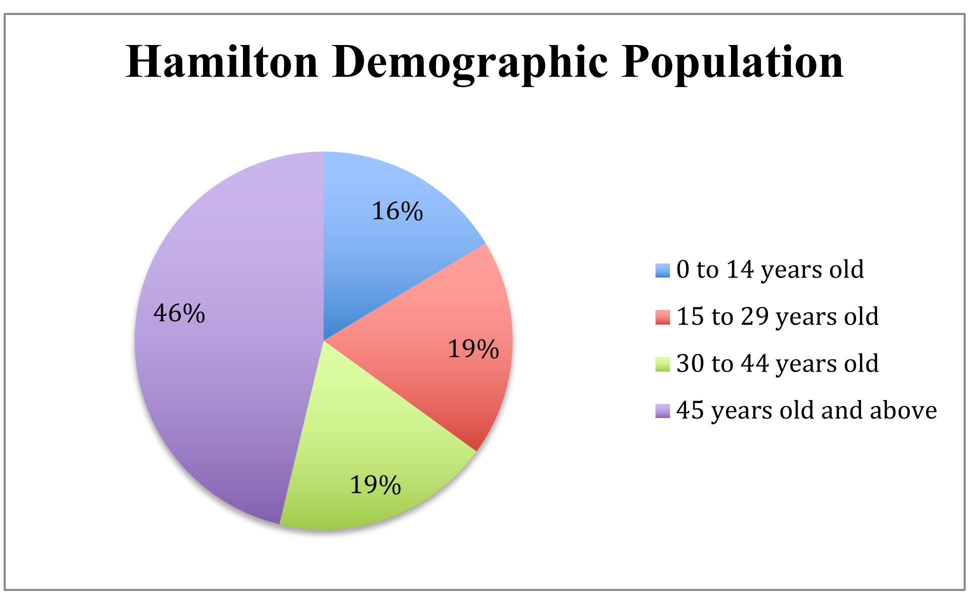


Figure 3



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