

Case: Franchising Gyms

Bain, Round 2

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Problem statement narrative

Your client is a gym franchisor. The client focuses on small gyms (approximately 3000 square feet) with standard fitness equipment, but no classes or lockers. The gyms are typically located in local strip malls. They are open 24 hours per day; members enter the gym via an access card. Staffing at the gym is minimal to none (depends on each individual franchisee).

This business is growing very rapidly. However, there is now a new competitor offering a similar franchising opportunity. To make our client's franchising opportunity more attractive, our client would like your input on how the profitability of its franchises can be improved.

Overview for interviewer

This is a straight-forward case. An ideal walk-through (presented in the subsequent slides) would include the following:

- Breakeven analysis based on understanding of revenue and cost structures
- Brainstorming of new revenue opportunities
- Brainstorming of cost cutting opportunities
- Analysis of pros and cons of market segments
- Conclusion / Recommendation

Case Type: Various

Information to be provided upon request

See following slides for further detail.

Potential Issue Tree & Approach to Solving the Case

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Candidate may propose analysis / action in:

Profit Structure (Rev and Cost)

- Key revenue streams
- Key fixed and variable costs

Possible follow-up and guidance to interviewer

- Should lead to next slide (the math question)

Market Opportunity

- Size of the market
- Growth expectations
- Key customer segments and differentiating qualities

Possible follow-up and guidance to interviewer

- Overall market expected to grow slightly faster than GDP given healthier living trends
- \$10 billion in revenue last year
- Relevant segmentation (location):
 - Urban
 - Suburban
 - Rural

Competitors

- Key competitors
- Amount of concentration or fragmentation
- By customer segments
- Key differentiating features

Possible follow-up and guidance to interviewer

- Key competitors offer essentially the same franchising opportunity client does
- Not a key aspect of the case; deemphasize

Question 1 – Breakeven Analysis

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Question

How many members must each gym location have to breakeven? This is a key metric for potential franchisees

Overall approach, data required and solution

- Identify the revenue per member, fixed and variable costs for a gym
- Monthly Revenue
 - Membership dues: \$40 / month
 - Vending machines (net): \$5 / month
 - Personal training (net): \$15 / month
 - Total: \$60 / month
- Variable Costs: None (or too minimal to matter)
- Fixed Costs
 - Rent: \$24 / square feet / year (or \$6000 / month)
 - Equipment: \$144K initial cost, 3 year depreciation, \$0 salvage value (or \$4000 / month)
 - Labor: 40 hours / week @ \$20 / hour (or \$3200 / month)
 - Utilities: \$400 / month
 - Franchise fee: \$300 / month
 - Marketing: \$100 / month
 - Total: \$14000 / month
- Breakeven calculation
 - Contribution margin: \$60 / month
 - Fixed Costs: \$14000 / month
 - # of members to breakeven = $\$14000 / \$60 = 233$

Information to provide up front

- Guide candidate to the approach
- Walk through each category (revenue per member, fixed and variable costs), brainstorming each of the potential associated line items
- Do NOT automatically provide each piece of data (such as salvage value for depreciation)
- Potentially tricky parts:
 - Using consistent metric (monthly, yearly, etc.)
 - Revenue = contribution margin because there are no variable costs
 - Asking for equipment salvage value
- Takeaway: By any measure, breakeven of 233 members is very low

Question 2 – Revenue Growth Opportunities

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Question

What are potential revenue growth opportunities the client can pursue?

Potential response

- Price:
 - Increase current revenue stream pricing
 - Tiered membership based on accessibility (time, equipment, etc.)
 - Consider multi-period contracts with discounted pricing
- Quantity
 - Increase # of gyms franchised
 - Increase # of members per gym (assume we have not hit a utilization saturation point)
- Create new product / service offerings
 - Juice bar
 - Sell clothing, timers, lightweights
 - Lockers for rent
 - Partner with full-service gyms to offer discount for classes (like yoga, spinning)
- Other
 - Increase marketing efforts

Question 3 – Cost Cutting Opportunities

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Question

What are potential cost cutting opportunities the client can pursue? What opportunities are more actionable?

Potential response

- Recognize that rent, equipment and labor are the largest expense categories, so start there
- Rent
 - Re-negotiate current contracts
 - Move to less optimal locations
 - Actionability: Low
- Equipment
 - Use the equipment longer (thus increasing the depreciation period)
 - Consider purchasing used equipment
 - Consider renting equipment
 - Consider consolidating equipment purchases to fewer vendors
 - Increase buyer power by making purchases across multiple gyms
 - Actionability: Moderate
- Labor (currently comes in 8 hours per day, M-F, to answer general questions)
 - Decrease the number of hours staffed
 - Utilize phone support
 - Post more FAQs on the walls
 - Actionability: Moderate

Question 4 – Segment Analysis

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Question

Which segment offers the greatest opportunity on a profitability basis? What are the key factors?

Potential response

	Costs for Franchisee	Gym Space Location Availability	Convenience for Members	Segment Fitness Interest	Segment Spare Income	Competition
Urban	High (☹)	Low (☹)	High (☺)	High (☺)	Medium	High (☹)
Suburban	Medium	Medium	Medium	Medium	Medium	Medium
Rural	Low (☺)	High (☺)	Low (☹)	Medium	Medium	Low (☺)

- Key Takeaway

- Rural segment is very attractive, because of the lower cost (rent, labor), high availability of gym space and low competition
 - Competition is the surprise factor; very few gyms have placed locations in rural areas due to very high breakeven membership requirements for fully-loaded, traditional gyms

Sample Recommendation

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Recommendation	<ul style="list-style-type: none">• Client business model allows for low breakeven membership point for franchisees• To improve profitability, client should consider revenue growth opportunities (give best examples) and cost saving opportunities (give most actionable items)• Client should also focus on the rural market segment, primarily due to a lack of significant competition
Risks	<ul style="list-style-type: none">• Adding new services (ie revenue streams) will make client gym offerings less distinct from traditional gyms• Cutting costs at a bare minimum gym may cause customer service issues
Next Steps	<ul style="list-style-type: none">• Execute on recommendations• Also consider M&A opportunities, primarily to gain scale and improve cost structure