

LUNCH N LEARN

Royalty Transaction: A Unique Liquidity & Monetization Strategy for Franchise Founders

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Speakers

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Options for Founders of Profitable Franchisors

- Status Quo
- Debt Recapitalization
- Private Equity / Sale
- Royalty Transaction

Introduction

- Diversified Royalty Corp (“DIV”) believes the **franchisor** business model is a **superior business model**
- Franchisors with proven store level economics, scale, profitability and with the potential to double their store count over time are **cash flow machines** – the operational leverage of the franchisor model, at scale, is awesome
- In the early 2000’s, the management team of DIV was working with several of North America’s best franchisors and invented a **unique royalty transaction** that generates a meaningful upfront liquidity event while selling no equity – providing the owners of these great businesses¹ a **far superior alternative** to selling to private equity

Why a Royalty Deal?

- It takes a **big effort** and often a long period of time to build a Franchisor to a point where it has achieved scale and becomes highly profitable
- Many entrepreneurs (owners) want to take some **money off the table** when their Franchisor becomes profitable
- Once a Franchisor achieves scale, the equity risk phase (while building to scale) is over – DIV believes owners of high-quality franchisors should retain **100% equity ownership** and reap the **economic rewards** of continuing to scale the business
- DIV's unique trademark and royalty transaction structure provides owners of high quality Franchisors with the liquidity of a private equity deal, while retaining **100% control** and **the economic upside** of continued new store growth
- Furthermore, the all-important **relationship** between the Franchisor and franchisees is **unaffected**, unlike a change of control private equity deal

Franchisor Attributes for a Royalty Transaction



Franchisor – stable annuity-like revenue streams
Robust store level economics
Strong new store growth prospects



Profitable – \$4+M of EBITDA
History of positive SSSG

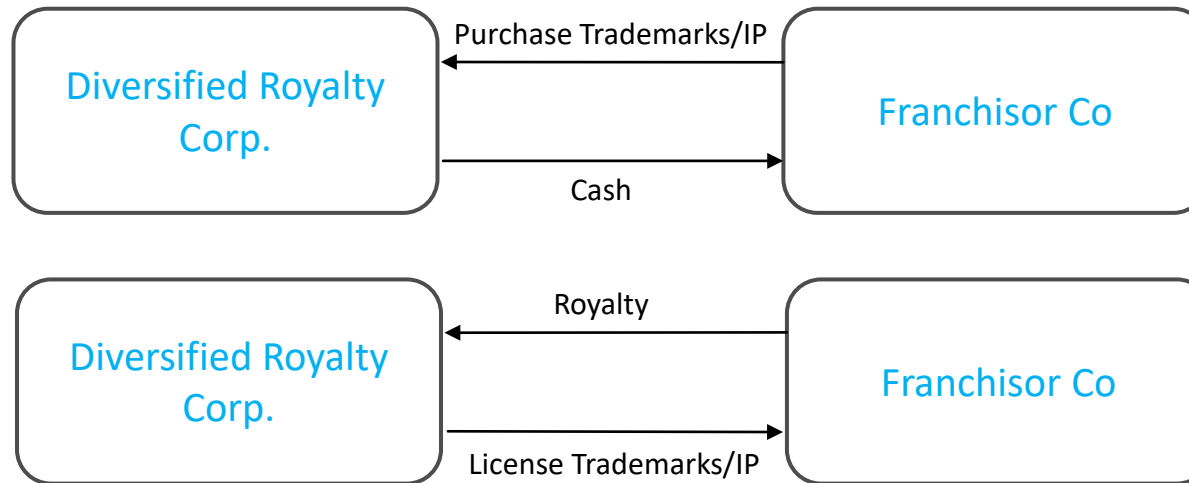


Amongst the market leaders in its category
Long operating history
Experienced management team

The royalty transaction is primarily targeted at **individually-owned franchisor businesses** that are **seeking a liquidity event** and **don't want to sell out** to private equity

How a Royalty Transaction Works

Step 1



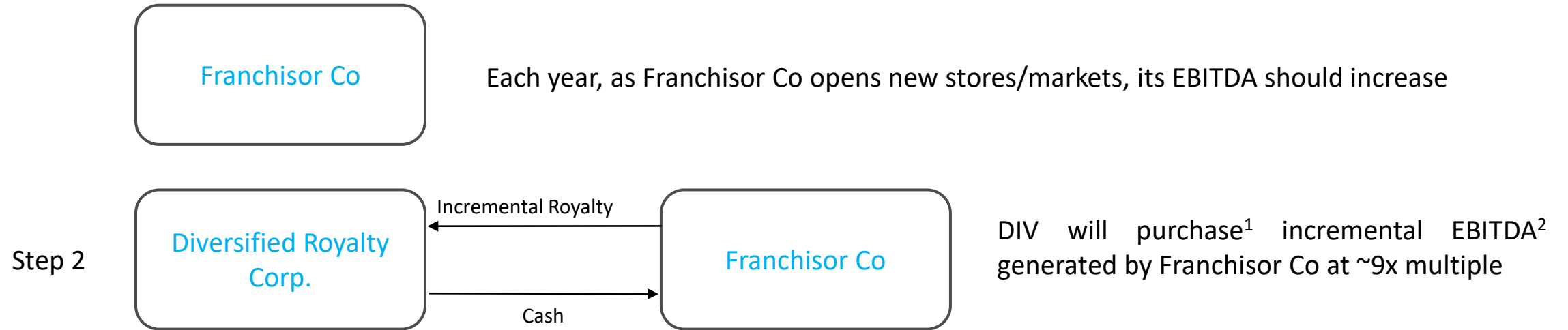
DIV purchases¹ the worldwide trademarks and IP for ~9x TTM EBITDA

DIV licenses the North American trademarks and IP in exchange for a royalty equal to approximately TTM EBITDA – the royalty would fluctuate based on SSSG or at a fixed rate

The owners of Franchisor Co:

- realize a **material liquidity event**
- retain **100% equity** ownership

How a Royalty Transaction Works



Since the owners of Franchisor Co own 100% of the equity, they are able to realize the benefit of **monetizing increased profitability** from continued new location expansion and operating leverage

Case Study – Boston Pizza



- While the initial royalty transaction creates a meaningful liquidity event, the cumulative proceeds from the sale of incremental royalties over time should dwarf the initial liquidity event – Boston Pizza provides a perfect case study
- Casual dining restaurant chain with 150 locations and ~\$10M of EBITDA
- In 2002, completed a royalty transaction and realized a **\$98M liquidity event**
- From 2002 to 2022, Boston Pizza opened 270 additional stores and **realized incremental proceeds of over \$400M**
- The owners of Boston Pizza have received **total proceeds of over \$500M** and they still own 100% of the equity!!

First US Royalty Transaction – Stratus



- Stratus Building Solutions (“Stratus”) is a franchise business operating in 69 markets, generating ~\$150M system sales and profitable – the outlook for Stratus is strong with continued double digit SSSG and opening up an additional 85 markets
- The Stratus owners were seeking a liquidity event, but with such strong growth prospects were reticent to sell controlling ownership to private equity – there was simply too much upside
- The Stratus owners were introduced to Diversified Royalty Corp and their unique royalty transaction at the IFA Convention in San Diego in 2022
- DIV and Stratus [announced the first US franchisor royalty transaction](#) on November 14, 2022

First US Royalty Transaction – Stratus



- A royalty transaction met all of the Stratus owners' objectives:
 - Meaningful **liquidity** event
 - Maintain **control** of the business
 - Meaningful **economic participation** in the continued growth prospects of the business
 - No change in **relationships** with its franchisees
- The owners of Stratus believe they can replicate the success Boston Pizza had with the royalty transaction

Founder Alternatives

Status Quo

Pro – retain 100% control

Con – no liquidity event

Debt recapitalization

Pro – retain 100% control

Con – modest liquidity – must pay back

Private Equity / Sale

Pro – significant liquidity event

Con – loss of control, investors run the show

Con – might not align with the founder's goals

Royalty Transaction

Pro – significant liquidity event

Pro – 100% ownership retained

Pro – participate in value of new store growth

Pro – manage timing of liquidity schedule

Diversified Royalty Corp

- DIV is acquiring a portfolio of trademarks and collecting royalties from high quality multi-location and franchisor businesses
- DIV is a ~\$650M business generating ~\$70M of royalty revenue from eight royalty partners



- DIV believes the [royalty transaction with Stratus](#) (the first US royalty transaction) combined with the royalty model being proven in the Canadian market over the past 20 years [will be a game changer](#) for US franchisors
- [DIV is actively looking to partner](#) with owners of great franchisor businesses

Summary

- Owners of great franchisor businesses in the US have been **programmed to think** their only source of meaningful liquidity is to **sell to private equity**
- Private equity has earned out-sized returns over the past 20 years buying the equity of great franchisor businesses
- DIV believes the franchisor business model is **superior** and owners of great franchisors **shouldn't have to sell their equity** if they want a large liquidity event and continue running their business
- DIV's unique royalty transaction provides owners of great franchisors with the **liquidity of a PE deal without selling any equity !!**

Questions

Thank You For Attending