

FERNWOOD NRG BUYS A HAIR SALON: A CASE STUDY

AS TOLD BY:

Lee Herrin, Executive Director, Fernwood NRG
Jacqueline Rogers, Owner, Studio 1284

DATE OF ACQUISITION: 2013/2014

LOCATION: Victoria, BC



INTRODUCTION



ABOUT THE BUYER

Fernwood Neighbourhood Resource Group (Fernwood NRG) is an enterprising non-profit organization run by and for the residents of Fernwood, a neighbourhood in Victoria, BC. The organization provides childcare programs, recreational activities, affordable housing, and community gathering spaces for residents of the neighbourhood.

ABOUT THE SELLER

Studio 1313 Hair Design was originally called Studio 1284. It was a community hair salon business and a gathering space for residents of the Fernwood neighbourhood. The original owner founded the business and ran it successfully with a team of experienced and professional stylists for 18 years before selling it to Fernwood NRG.

OVERVIEW



In 2013, Jacqueline Rogers, owner of the business, and long-term friend and ally of Fernwood NRG's Executive Director, Lee Herrin, approached him in a crisis. She had just had a falling out with her landlord and was worried that she would have to close her business as a result.

Herrin initially proposed that she could rent a new space for her business in a building that Fernwood NRG already owned. Rogers appreciated the offer, but she was planning on retiring in a few years and did not want to take on the risk of signing a new lease and renovating the space.

Herrin still wanted to help preserve the business, so he sought permission from the Board of Directors of Fernwood NRG's subsidiary company to propose that the organization buy the hair salon, with one caveat: the previous owner would stay on as Manager for a few years during the transition. Fernwood NRG had acquired property and started a business in the past, but they had never acquired an existing business. This was a first for the organization.

When Herrin proposed the idea to Rogers, she was excited. After taking some time to think it over, she decided to proceed with the offer.

At the time of the acquisition, the business value was in the goodwill of the business, the staff, and the inventory. As a result, the two parties were able to work out a deal that focused on a management contract and not on the purchase price.

Following the acquisition, the timeline moved rapidly. Fernwood NRC renovated the new space to outfit it as a hair salon and reopened the business as Studio 1313, about a block from its original location. All of this happened within three weeks.

With the management contract in place, the previous owner continued operating the business with little oversight, as she already had experience running a successful hair salon.

The word got out about the new ownership, and more staff were hired. Studio 1313 Hair Design was able to continue to operate in the community, increase its revenue and maintain valuable local employment opportunities.

MOTIVATIONS

Although neither party was actively seeking out acquisition opportunities, they could recognize and respond to the opportunity as it presented itself.

THE BUYER

- Preserving an important local business in the community
- Creating an additional revenue stream that could fund the organization's community programming
- Filling space in the organization's building with a successful, long-term, neighbourhood business
- Increasing Studio 1313 Hair Design's positive social and environmental impacts.

THE SELLER

- Preserving the business in the community without having to take on the risk and commitment associated with signing a new lease
- Maintaining employment for herself.
- Maintaining employment opportunities for staff.



ACQUISITION DETAILS

PURCHASE PROCESS

In this case, the preparation process was fairly informal and minimal, partly because of the short timeline and because Fernwood NRG's Executive Director and the business owner already had an excellent relationship. No legal, accounting, or consulting work was required. The deal was sealed with a handshake between the two parties.

The previous owner prepared the books and shared them with Fernwood NRG. She was a sole proprietor who had never planned to sell her business and had not prepared financial statements because she had not needed them. Theoretically, this represented a risk, but Fernwood NRG was focused on the revenue and cost structure, which the previous owner could easily explain to them.

Fernwood NRG created a financial model for the business based on past revenue and a few key assumptions: they assumed Fernwood NRG would be able to manage costs but also increase revenue and prices in the new space. Based on those assumptions, they were able to model different scenarios for the business and forecast future profitability.

A management contract for the previous owner was negotiated, as were wages and benefits for the existing staff. The management contract was incentivized based on sales growth. Fernwood NRG offered ongoing employment to all of the existing staff, but not all of them accepted because they didn't fully understand what the acquisition meant for the future of the business.

DEAL STRUCTURE

Fernwood NRG is a charity and is the sole shareholder in a subsidiary company, which they used to acquire and hold the business.

The deal was structured as an asset purchase, which meant Fernwood NRG's subsidiary company bought the inventory and chattels of the business rather than the shares or brand of the company. Fernwood NRG paid \$5,000 to purchase the business, plus a management contract for the owner. They put in \$25,000 for space upgrades. The acquisition was self-financed.

The previous owner signed a two-year management contract to manage the operations. This also ensured that the business's goodwill attached to the previous owner carried over in the transition.

Sales dropped in the first few months after the acquisition because the business lost some staff. Once Fernwood NRG hired more stylists and began promoting the business, sales rose steadily. Revenue grew substantially in the first few years, from around \$12,000 per month in 2014 to \$30,000 per month in 2018.

Profit margins are around 15%, making this a healthy small business.



KEY CHALLENGES

THE BUYER

- Some of the staff left during the transition, which made the process more difficult because much of the goodwill and value of a hair salon lies with its staff.
- Due to the novelty of the idea, in the initial stages of the acquisition, it was challenging for the Executive Director, who championed the deal, to demonstrate to Fernwood NRG's staff and board members that the acquisition represented a good opportunity for the organization as a whole.

THE SELLER

- After the acquisition, it was initially difficult for the business owner to adjust to becoming an employee who had to report to an external manager regarding critical decisions rather than making executive decisions independently.

KEY SUCCESS FACTORS



THE BUYER

Keeping the previous owner on with a management contract was key to a successful transition.

It ensured that the goodwill, reputation, and sector-specific knowledge attached to the owner stayed with the business as it transitioned ownership.

THE SELLER

After the initial adjustment to being an employee, the fact that Fernwood NRG trusted Rogers' abilities and gave her the freedom to run the business was critical.

It enabled her to successfully get the business to the point where it could run itself under Fernwood NRG's ownership before she retired.

LESSONS LEARNED

THE SELLER

- Rogers calls the acquisition the "perfect exit strategy" because it preserved the business and employment opportunities in the community.

THE BUYER

- Identifying the right management, who will bring the same passion to the position as the original founder, is important if you want to continue operating a business "as-is."
- It can be risky for an organization to purchase a business only to run it off the side of someone's desk. However, if the purchasing organization has staff with the capacity and capabilities required to run a business, an acquisition can generate income to help support its mission..

OUTCOMES

The acquisition meant the previous owner didn't have to lay off her staff. It allowed her to preserve her business and staff's jobs and continue serving the community.

After the acquisition, Studio 1313 became a Zero Waste business. It now offers a line of eco-friendly products and non-ammonia colour treatments.

The stylists now participate in a youth training program that teaches students from a nearby high school how to cut hair. The salon also supports low-income high-school graduates by providing them with affordable updos for their graduation ceremonies.

Profits and rent from the space go back to Fernwood NRG to support the organization's community programming. People from the neighbourhood like the idea that their money goes back into supporting the community when they get their hair done at Studio 1313.



Photo: Studio 1313 Facebook page