No One Does It Like Frisby Does It

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Abstract

This case study discusses the acquisition of Pinky, a direct competitor of Frisby. Frisby was a Colombian breaded and fried chicken restaurant chain with a strong and very particular organizational culture, 130 restaurants, and annual sales of US$42 million. Despite the 2009 world economic crisis the fast food restaurants industry had become very dynamic particularly in Colombia and was attractive to foreign investors and multinational companies. General Manager Francisco Guzmán was analyzing the option of buying Pinky, a competitor located in the city of Medellin that had generated important brand blunders and now facing market share losses.

That afternoon, in February 2010 in the city of Pereira, Colombia, was like any other. Frisby's senior management team was meeting with the company's founding partners, Mr. Alfredo Hoyos and his wife, Mrs. Liliana Restrepo, in the board room at the company headquarters in the Dosquebradas district. Mr. Francisco Guzman, the General Manager, was leading the meeting; the room was tense. They needed to decide whether to buy the Pinky Company, which had been a problematic competitor with a peculiar history in the city of Medellin. Frisby's management was evaluating the possible purchase meticulously and carefully since sales in the city of Medellin represented almost 30% of the company's total sales, and Pinky had been the cause of enormous brand confusion in the market.

Frisby was a Colombian company that sold breaded and fried chicken in Colombia. In 2010 the company had 130 restaurants throughout the country. Annual sales were approximately $42 million. They directly employed close to 1,300 people and generated an additional 4,000 jobs indirectly. They had acquired two franchises: Cinnabon, a franchise from the United States that sold cinnamon buns and coffee and was currently growing, and Sarku Japan, an Asian restaurant from the United States, which was newer.

The Birth of an Industry and a New Company

Alfredo Hoyos remembered with pleasure how this great adventure had started and the history of what today was known as Frisby.

In the 1930´s his father studied engineering in Bogota. While he traveled by bus to his home in Antioquia, an engineer told him it was hard to make a living in their profession, and he managed to get by thanks to a small supermarket. He assured Alfredo's father that the money was in the business, and particularly, in retail. After that conversation his father decided to leave college to start a business. Alfredo's grandfather did not approve of his decision and told him that if he left college, he must also leave the house. In 1935 Alfredo's father left home and went to the city of Pereira to try his luck.

In Pereira his father got a job as an assistant in a fabric store called *Almacen Real*. After a few years the owner wanted to retired and sold the store to his father, he finally became a businessman. Under his father's leadership the store began to grow and prosper. Alfredo remembered that his father liked to learn and read about topics that were of his interest, unlike the traditional education system. One of the things he decided to learn was English. As the business grew his father hired his siblings at the new stores they opened to help him run the business.

Once, his father traveled to Japan to buy toys. In Japan he was invited to one supplier's farm and discovered something completely new to him: a chicken incubator. He became interested in the technology and thought it would be interesting to explore the business because of its market potential in Colombia and the economic and social benefits that it could bring to the population. In 1948 chicken was one of the most popular proteins consumed in Colombia. However, chicken processing was rudimentary, and generally, farms could not guarantee sanitary conditions necessary to maintain quality.

Soon after, he began using the technology on one of the family's properties, thus founding the first chicken incubator and industrial processing company in Colombia. Over time, the business grew to become a point of reference in the industry.

Alfredo was involved in his father's business from early on. He studied at the *Colegio La Salle* high school in Pereira and, like his father, never completed college.

Alfredo commented:

"I was exposed to an entrepreneur's life, and I was also exposed to quality literature found in the library at my house: European classics, like Alexandre Dumas, Stefan Zweig and many other philosophers, who later formed a core part of the business culture we created in the company".

After an epidemic on the farm, his father traveled to Dr. Salisbury's clinical laboratory in Indiana in the United States to become trained in avian pathology. He took advantage of the trip to participate in various practicums on several avian farms where he learned about best practices in the industry that were much more advanced than the ones practiced in Colombia. After his training he saw an opportunity to represent the laboratory in Colombia. Upon his father's return, Alfredo worked with his father to distribute medicine and animal nutrition supplements, which allowed him to maintain close contact with the avian industry, in general.

In 1967 Alfredo founded Pimpollo, a chicken processing plant; this marked his first experience in the avian industry. Pimpollo was located in the province of Risaralda in Colombia and grew to become one of the largest distributors in the region. Supermarkets and restaurants were some of its main customers, in particular, the roasted chicken restaurant, Kokoriko, which was a leader in its industry. Despite his success, in 1970 Alfredo decided to sell Pimpollo to the Kokoriko restaurant chain. He became a shareholder as part of the sale, a status that he retained for a few years.

Alfredo met Liliana Restrepo during his time with Pimpollo after divorcing his first wife. Liliana commented:

“When we met, we discovered that we complemented each other in many ways, and that’s how Frisby was born: through a combined energy. It has made a significant difference”.

After selling Pimpollo Alfredo decided to take some well-deserved vacation time and read the newspaper every morning from his office. However, he soon became bored and decided to look for a new venture. It was the 70s in Pereira, and contact with the outside world was minimal. Alfredo remembered:

“Because I had lived in the United States, I used to eat at pizza places. When I was still dating Liliana, we decided to open a pizza place in Pereira. We got a restaurant in front of the Parque del Lago and we started-up our pizza business. We have always liked doing things well, so we settled on a name that alluded to pizza and we brought a pizza chef from Bogota to make the best Italian style pizzas”.

The pizza restaurant was a hit. Alfredo had put the pizza chef in front of a window so that people could watch him stretch the pizza dough and throw it in the air. This attracted visitors to the park, and people began calling them “the flying arepas” for the way the dough was tossed. As a way to innovate and offer better customer service, Alfredo introduced new products. The first was Helados Mimo's, a Medellín ice cream shop that Alfredo represented in Pereira.

Alfredo constantly looked for ways to improve his restaurant. He regularly attended international food fairs. On one of his trips, he found that breaded and fried chicken was booming in the United States; he was attracted by the business opportunity since he had experience in the chicken industry. One of the machines that most interested him was the pressure fryer. These machines allowed the chicken’s juices to flavor the meat as it cooked by increasing the boiling point of water. This technology was not yet available in Colombia, so he decided to bring it to Pereira and enter the breaded and fried chicken market.

Alfredo remembered:

“We brought the special fryer from North America and installed it in our kitchen. My wife and I began to do taste testing with our friends every day until we found a recipe that everyone liked”.

At that time customers in Pereira clearly preferred roasted chicken. Several acquaintances of Alfredo and Liliana's warned them that the business would flop since the market was dominated by roasted chicken companies, such as Kokoriko. Alfredo and Liliana trusted in their recipe.

As Liliana stated:

"Alfredo and I created the recipe. We prepared it at night, leaving the chicken to marinate, and we were the ones who served our clients".

Alfredo commented:

"Our customer service was our main differentiating factor. We always understood that our success depended on our clients. We served extended families, who came all together to enjoy a tasty meal".

Contrary to what their acquaintances had predicted, the business did pretty well and was widely accepted by the people of Pereira. That success led Alfredo and Liliana to grow the business. Soon, the restaurant at the *Parque del Lago* became a sensation, the recipe was accepted and breaded fried chicken became a success and began to replace pizza.

Frisby

The company's first restaurant in *Parque del Lago* in Pereira began to have success. Fried chicken was becoming fashionable in Pereira, and sales grew rapidly. Motivated by their success and the restaurant's popularity, Alfredo and Liliana decided to open a second location. The decision to open the new restaurant was limited by the location, which had to be in a nearby city, since the company only had three employees at the time: Alfredo, Liliana and a person responsible for accounting. The restaurants had to be managed by Alfredo and Liliana, and probably some other employee would be hired to help with the cooking. Considering these factors, they believed it would be convenient to expand to the town of Armenia. Since it was located nearby, they believed they could easily manage both restaurants.

The second restaurant, like the first, became quite popular among local residents. It soon became necessary for them to hire more people to help manage and operate the restaurants. Once the second restaurant opened, the need for additional personnel became evident. As the company grew, its human resources became key to Pollo Frisby's development. Alfredo commented:

"From the beginning Liliana was the one who took care of personnel issues, and I was in charge of quality control, research and product innovation, or the technical part. In terms of personnel, we have always believed that customer service needed to be excellent. The way to offer good customer service to clients was making sure that our employees were motivated and completely happy".

The company' growth, for the most part, had been organic and close to Pereira in the region known as *El Eje Cafetero* (The Coffee Center in English), which included cities, such as Armenia, Manizales and Cartago. As the company's number of restaurants increased, its organizational structure also grew to support the business and manage its complexities better.

The organizational structure was developed to support the company's growth. They created departments in order to have control over operations, while ensuring that they provided clients with the best quality and service possible. Likewise, they developed internal administrative control processes and technical operations to standardize how they did business. All of these procedures gave rise to the Frisby System. The Frisby System was a series of steps that described how to operate and manage a new restaurant, in addition to suggesting specific distributions for the kitchen and how to train personnel. It also stated Frisby's mission, vision and values, or the company's general culture.

At the beginning of the 80s, Frisby was available extensively in *El Eje Cafetero* and was growing at any interesting speed. Frisby's success, growth in sales and greater geographic coverage led several people to show interest in franchising the restaurant across Colombia and abroad; however, Frisby was not franchised at that time. Alfredo commented:

When a company thinks about franchising, it has to be compatible with the company culture. If the company culture and franchising don't align or bode well, there's a problem and the relationship is destined to fail. Companies that offer franchising have to be mature, have established controls and be able to stipulate a fair relationship for both sides. That's why before offering franchises we wanted to practice in a controlled environment, perhaps with the family.

One of Frisby's growth plans included opening in the city of Medellin, an untouched market at that time; however, they were not sure how they should start operations there. In 1983[1] Alfredo and the management team entered Medellin through a franchise concession to a family friend. They created a company that was responsible for implementing the so-called Frisby System in the restaurants. Frisby was in charge of transferring know-how, best practices and the Frisby culture to the franchise. During the first year of operations of Frisby's franchise in Medellin, they opened six restaurants. Given the

[1] Source: www.notinet.com.co/pedidos/3939.doc, viewed March 2014.

public's favorable response, the family also opened their own restaurants in Medellin; they served as a primary source of information about how the market was behaving.

Frisby's geographic expansion continued to Cali where the family opened its own restaurants. Their growth plan was aggressive. By December 1989[2] they had opened their first restaurant in Bogota, located on 122nd Street between 15th and 19th Avenues. Francisco Guzman said:

"The experience with Frisby's restaurant in Bogota was interesting. The first clients were people who lived in Bogota, but were from 'El Eje Cafetero' or Medellin; they knew us. This helped drive the growth of our restaurant in Bogota. It was mainly through client word-of-mouth".

Frisby's growth continued and reached double digits in the 90s. In 1997 Frisby had 51 restaurants in 9 of Colombia's main cities.[3] In 1998 they expected to open three more restaurants: two in Medellin and one in Ibague. In 1998 they also had an opportunity to open in San Andres through the purchase of a company called Rico Mac Pollo. The company had been founded by a couple of entrepreneurs in San Andres. The owners had legal problems because of their name and could not operate normally,[4] leading the company to a precarious financial situation. After an intense negotiation process, Frisby decided to purchase the brand. Afterwards, Frisby faced several problems, including poor habits developed by personnel, difficulty in managing the operations from afar and the poor condition of the restaurants and equipment. The integration process was tedious and long.

Soon after, in 1999, Colombia experienced one of its most severe economic crises in recent history. Colombia's growth rates prior to the crisis surpassed 4%,[5] but by mid-2000 its exchange rate had fallen approximately 4%.[6] This fall impacted unemployment rates, which reached unprecedented levels of almost 20.4[7]%. The crisis, at first, was due to problems in the banking sector. As a reaction to the crisis, people changed their consumption patterns and limited unnecessary expenses. One of the main areas affected was dining out. This situation had a direct impact on Frisby's sales. Frisby's institutional

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[2]Source: http://www.revistalabarra.com.co/ediciones/ediciones-2010/Edicion-38/portada-21/frisby-conocer-al-cliente-su-obsesion.htm, viewed March 2014
[3] Source: http://www.eltiempo.com/archivo/documento-2013/MAM-642200

[4]Source: http://www.eltiempo.com/archivo/documento/MAM-47667 viewed March 2014
[5] Source: Arias, Andrés: "The Colombian Banking Crisis: Macro Economic Consequences and What to expect", UCLA 2000
[6] Idem
[7] Idem

efforts focused on integrating the newly-bought Rico Mac Pollo. The company was in a vulnerable position and had been severely affected. Because of this situation, the senior management had to respond. Liliana Restrepo remembered:

"We discussed the situation we were facing. We knew that we had to make changes, but we didn't want to cut people even though that was the easiest way to cut the company's fixed costs and continue operations. We didn't want to get rid of Frisby's family. So we decided to look within the organization, study our processes and find the way to make them more efficient. That required a lot from our staff. Our need for this commitment led us to organize a tour of the country to meet with all of our staff. The idea was to share the seriousness of the situation and ask for their commitment to the company to be able to move forward".

Rico Mac Pollo's culture was different from Frisby's, and the people who had worked there had, in Francisco Guzman's words, bad habits that could affect the organization. After several months of trying to integrate the companies, Frisby decided to sell that portion of their operations. This decision caused discontent and mistrust among managers. Luckily, Frisby was able to make their processes more efficient, which allowed them to reduce operating costs and remain productive.

Frisby boomed in the years after the crisis. They restructured operations and the reengineering paid off; after the crisis Frisby had some of its best years in history.

Organizational Structure

In 2009 Frisby had sales of 81.742 billion Colombian pesos,[8] making it the number one competitor in the fried chicken market. Frisby had adjusted its structure as it grew and incorporated industry best practices. It had 131[9] restaurants in the country and planned to open 4 more the following year. Exhibit 1 shows the company's organizational structure. The organization also had different business units that the headquarters supported through accounting and payroll; however, operations were independent. The business units at the time were: Frisby, Cinnabon, Sarku Japan, the Alfredo E. Hoyos agro-industry Company and Frisby Foundation.

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[8] The representative exchange rate was 2,044.23 Colombian peso per United States dollar on December 31, 2009, Banco Central de Colombia http://www.banrep.gov.co/es/trm.

[9] Source: http://www.elcolombiano.com/BancoConocimiento/F/frisby_pico_primero_y_se_quedo_con_pinky/frisby_pico_primero_y_se_quedo_con_pinky.asp viewed May 2014

Frisby had been managed by its founding partners and family members. At first, Alfredo, the company's founder, had been its General Manager, responsible for innovation and technical development. In 1998 Liliana became General Manager, in addition to her role managing human resources. After Liliana, Alfredo's nephew, Felipe Lopez Hoyos, took over as General Manager. He led the company until 2005 when it became a franchise Francisco Guzman was the company's first General Manager who was not a family member. He had previously served as the company's Chief Financial Officer.

To retain greater control over the restaurant chain, they divided the company internally into four regions (see Exhibit 2); the franchise division was managed separately. Each region had a regional director who was responsible at the macro level. They each had area chiefs or managers who supervised between five and seven restaurants. The area chief was responsible for everything at the restaurant, including quality, branding, restaurant inspections and, of course, sales. Each restaurant had its own restaurant manager who was in charge of day-to-day operations and the restaurant's performance. Frisby was headquartered in Dosquebradas, where operations control took place. There, they had a vegetable and fruit processing plant and product development laboratory with the most advanced technology in the market. The factory supplied the restaurants' needs for side dishes, such as salads. Plantains were distributed by a logistics supplier that had agreements with the company for distribution, inventory management and, in some cases, processing. Francisco Guzman said:[10]

"We turned over some processes to experts so that we could dedicate ourselves to the essence of our business, which was serving customers so that they had an excellent experience in service, quality and flavor: the brand's three customer pillars".

Chicken was mostly purchased from suppliers operating in the different regions, which allowed the company to access fresh chicken and reduced logistics costs. They maintained close relationships with those suppliers. Some processing to prepare the cuts of chicken needed for the dishes on the menu were done directly at the suppliers' facilities or at logistics centers. When this was needed, a Frisby employee was assigned to the logistics center and was responsible for training the supplier's staff, verifying quality processes and maintaining sufficient inventory to satisfy demand. All Frisby products were elaborated using fresh chicken; chicken was never frozen, so as to maintain high quality products for clients. In addition, they never used processed or reconstituted chicken for their dishes. All dishes were made using special cuts that allowed them to maintain consistency and flavor. For example, chicken nuggets were not made of ground, reconstituted chicken; rather, they were made from special cuts of chicken breast.

[10] Source: http://www.revistalabarra.com.co/ediciones/ediciones-2010/Edicion-38/portada-21/frisby-conocer-al-cliente-su-obsesion.htm viewed May 2014

One way that allowed them to serve customers better was to understand client needs and innovate constantly to respond to those needs, both in terms of service and product lines. The company had a department of innovation that reported directly to Alfredo, the President. The department was managed by a chef from Pereira who had studied in Bogota. Francisco Guzman commented:

"Constant innovation was one of Frisby's main characteristics. We innovated in packaging, in products and in ways to reach our clients. Just in the last year, innovations represented 30% of the group's sales. Innovation was done together with senior managers even though there is a department of innovation led by Alfredo and Sebastian (the chef); that department does technical and culinary innovation. However, innovation requires greater development. You have to evaluate how it will be processed, the price model, the packaging, the way to market it and results from focus groups that test the product. At the end the innovation comes from the company as a whole".

Alfredo mentioned:

"Innovation is part of our company; however, innovation isn't worth anything if it doesn't respond to a market need. It doesn't make a difference if you have a new product, if clients don't want it".

Innovation was not limited to customer service; it was also applied to the company's processes. One of the company's most innovative departments was the department of information technology. Information was managed using a software system that had been tailor-made by the company's department. Pollo Frisby was a pioneer in Colombia in developing that type of system. The system allowed Francisco Guzman, the General Manager, to receive sales data on a daily basis and see how each restaurant was performing. The department of information technology had also developed other key services for the organization, such as a service management call center platform that was based in Medellin, and a system to order online through the "Delivery" system, which represented 30% of Pollo Frisby's sales.

Organizational Culture

Frisby's organizational culture was particular in that it focused on developing each employee that formed part of the Frisby family. Frisby focused on providing clients with a quality experience, meaning both in the customer service they offered, as well as the products that were consumed. Product quality was guaranteed through the company's operations and continuous training in technical areas. However, the focus on a unique customer experience was harder to achieve. Francisco Guzman commented on the company's commitment to its human resources:

"We're people serving people, and we're also people who work when others are sleeping".

Alfredo stated:[11]

"At Frisby we lead by creating awareness. We teach people psychology, philosophy and ethical principles. There isn't another company that works using this system to develop awareness among its staff. Today, you hear a lot about a knowledgeable and informed society, but what is important is self-awareness and developing that. One of our foundational beliefs is that of philosopher Martin Buber, who speaks of "freedom and destiny," meaning internal freedom, freeing ourselves from the chains that we bring with us with our past, with limiting thoughts that we are taught as children, from our families, at school, church, all of which build dark areas in our subconscious that are called denied spaces. So, the evolution of awareness isn't anything but discovery of those denied spaces that we have and bringing them to our consciousness and integrating them into the system. That is what developing awareness is about, and that is what we try to teach to all of our staff".

The company has tested and shared several philosophies and activities, including Suani, neurolinguistic skills, coaching and bio dance. Exhibit 3 provides a more detailed list of activities. These activities had been used regularly by the company with its employees. Liliana commented:

"Alfredo and I continuously look for ways to become better people and we've come across several philosophies and techniques that we consider to be very important. We try them out first in our personal lives, and if we think they're good and they help us: why not share them with our employees?"

Alfredo and Liliana learned several activities (Exhibit 4) and applied them in their lives. They learned about different philosophies and researched those types of life methodologies.

Frisby also institutionalized customs as part of its culture, which helped develop the company. *Five Minute Meetings* were held at each restaurant every morning for five minutes as reflective motivation to start the day, share news and coordinate the day's tasks. Another custom was the *Primary Group* tours, which were monthly meetings at the administrative level at each restaurant in which participants had breakfast and learned about the performance of the company and each job position, as well expectations for improvements. They also promoted *Management Tours* in which

[11] Source: http://www.revistalabarra.com.co/ediciones/ediciones-2011/edicion-49/personajes-2011/alfredo-hoyos-presidente-frisby.htm viewed May 2014

the General Manager traveled to every restaurant to talk about the company's direction, achievements and future challenges with employees in order to maintain open and constant communication within the company. Another regular communication channel that had been institutionalized was conversation opportunities with the founding partners in which both sides could converse about concerns and expectations.

Economic Outlook

In 1999 Colombia faced one if its worst economic crises due to exchange rate tension, among other issues. In 2000 the economy began to recover slowly resulting in the country's GDP per capita doubling in a period of less than 10 years. Slowly, the country began to recover with its annual GDP growth equally more than 2% by 2008 (see Exhibit 5). Unemployment dropped from 17% in 2000 to 12% in 2009, contributing to greater income and increased purchasing power since the country's consumer price index remained low (see Exhibit 6).

Different sectors of the economy contributed to the GDP in different ways. Exhibit 7 shows how some sectors grew more than others. The hospitality and restaurant services sectors grew little, but became more important. In the fourth quarter of 2009 restaurant services grew 0.4%, due to the effects of the global financial crisis; however, and in general, the sector was growing. This trend was promising for restaurant businesses and service providers. Between 2004 and 2008 the restaurant sector grew approximately 6% annually, and in 2007 it was the Colombian industry with the greatest growth, of 5.95%.[12] This growth was due in large part to changes in consumer patterns and lifestyles in Colombia. Since 2000, unemployment had decreased in the country, going from 17% in 2000 to 12% in 2009. An increase in employment meant more people went out to work, and, as a result, food consumption outside the home increased by approximately 150%.[13]

According to the National Statistics Administration Department, in 2009 approximately 12.7% of registered businesses belonged to the hospitality and restaurant sector. Even though the sector was booming, there were still some challenges, such as guaranteeing sanitary conditions in kitchens, offering a range of healthy dishes at accessible prices and

[12] Source: Turbulencia empresarial en Colombia: sector restaurantes comidas rápidas: Kokoriko, Frisby y la brasa Roja / Juan Pablo Roa Martínez [et al.].— Centro de Estudios Empresariales para la Perdurabilidad – CEEP, Facultad de Administración, Universidad Colegio Mayor de Nuestra Señora del Rosario. Bogotá: Editorial Universidad del Rosario, 2011 p.9
13 Idem

professionalizing the sector. The size of the restaurant market in 2009 was estimated at 15 billion Colombian pesos,[14][15] distributed geographically as shown in Exhibit 8.

The fast food industry in Colombia, and in Latin America, in general, included micro and small enterprises, which were usually family businesses and sold homemade and fast food as a means of subsistence. Many of these businesses operated informally, resulting in lower operating costs because they did not pay taxes or social security. In some cases they did not even meet minimum sanitary and quality standards.

Per capita chicken consumption in 1998 was 11.2% and grew to 21.6% in 2008. Prices ranged 15 to 20% less than beef. Because chicken was a cheap and healthy protein, it was preferred by Colombian consumers. This preference led, as mentioned, to the existence of many independent shops selling chicken, mostly roasted over a fire. There was plenty of competition among fast food establishments in different segments, including hamburgers, pizza, roasted chicken, fried chicken, sandwiches and Mexican food. However, Colombian consumers clearly preferred two types of hamburgers and chicken. In 2009 TGI[16] (Target Group Index) reflected a clear preference for fast food restaurants serving chicken. Included in the group were Frisby, Kokoriko and La Brasa Roja. However, when measured by sales, hamburger restaurants, such as El Corral and McDonald's, sold more, with sales[17] of $84 million and $72 million, respectively.[18]

Colombia's conditions, at that time, made it attractive to foreign investors looking for greater profitability than in the United States, which was in the midst of its economic crisis. During President Alvaro Uribe's administration, violence was greatly reduced from 68.9 homicides per 100,000 inhabitants in 2002 to 33.7 at the end of 2009. In addition, the exchange rate during that same period remained quite stable. Inflation fluctuated around 5%. In the 2009 Ease of Doing Business Report Colombia was ranked 53 out of 181 countries, after having improved its position by 13 spots.

Many foreign companies entered Colombia through franchises, which was not a new phenomenon. In fact, the first franchise in the country was Burger King, in 1983;[19] however, it left the market in 1989 because of low sales, waves of

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14 Source: Presentation: El Sector de la Hospitalidad en Colombia, Consultora Raddar.

15 The representative exchange rate was 2,044.23 Colombian peso per United States dollar on December 31, 2009. Source: Banco Central de Colombia, http://www.banrep.gov.co/es/trm.

16 For additional information see www.revistalabarra.com.co/ediciones/ediciones-2010/edicion-40/top-100/batalla-de-pollos-y-hamburguesas.htm

17 For additional information see http://lanota.com/index.php/CONFIDENCIAS/Ranking-cadenas-de-comida-rapida-de-Colombia.html

18 Ídem. Data calculated using sales figures from companies in Colombia.

19 Source: http://www.dinero.com/edicion-impresa/caratula/articulo/la-llegada-mcdonalds/182503

violence and the inability to repatriate capital to headquarters.[20] In 1995 McDonald's decided to enter the market; in its first year of operations with an investment of nearly $75 million, it opened 12 restaurants. By 2008 it was the country's largest fast food chain in terms of sales. Other franchises also entered the market during this period, including Burger King, Kentucky Fried Chicken and TelePizza. McDonald's had plans to grow 20% in sales in 2010 and open 7 more restaurants in the country.[21] In addition, it was rumored that other actors would be entering the market because it was so attractive.

Competition

Francisco Guzman commented:

"We compete for Stomachshare[22] in our business; in other words, we compete to feed people. People usually eat three times a day and that is the only thing we have to compete. Competition is stiff because we have to compete against other restaurants, arepa stands and hot dog stands in the street. Colombia's informal food industry is really big. We think that it's between 15 and 20% of the industry,[23] and they compete with lower costs because they don't pay taxes. They also lack quality control processes, sanitary conditions and standardized processes, which makes them more risky for the population".

There were several fast food options, from hamburgers, roasted chicken, fried breaded chicken, sandwiches, Mexican food, pizza, Chinese food, to of course, the informal sector. The main hamburger competitors were:

Hamburguesas El Corral, a Colombian owned company that was founded in 1983 in Bogota. Its main product was self-served hamburgers. In 2001 it diversified and started Corral Gourmet that offered a range of premium products and a sit-down restaurant dining experience. In 2004 it started a new option called Beer Station where clients could enjoy a large variety of artisanal beers. El Corral operated 160 restaurants in 25 cities in Colombia. It also operated in Panama, Chile and Ecuador through franchises.

McDonald's began operations in Colombia in 1995 with the opening of its first restaurant in Bogota. During the first year of operations, it opened another 12 restaurants with an investment of close to $75 million. In 2008 it was Colombia's

[20] The Government of Colombia had placed restrictions on repatriating capital to headquarters.
[21] Source: http://www.revistalabarra.com.co/ediciones/ediciones-2010/edicion-40/top-100/mcdonald-s-el-numero-uno-en-ventas.htm
22 Terms used by the General Manager to refer to the portion of the market limited to feeding clients.
[23] Source: http://www.revistalabarra.com.co/ediciones/ediciones-2010/edicion-40/top-100/batalla-de-pollos-y-hamburguesas.htm

largest restaurant in terms of sales at the three companies it owned. It became the first non-Colombian restaurant with that status.

Frisby's competition in terms of chicken restaurants differed. The three largest competitors were Colombian companies: Kokoriko, Frisby and La Brasa Roja. One of the most important cities in terms of chicken consumption was Medellin, which represented 10.4% of all fast food restaurant sales in Colombia. Medellin was home to a company that had once been a strong competitor to Frisby, but whose position had weakened: Pinky. Pinky only operated in Medellin. It had 17 restaurants in town. Medellin represented 30% of Frisby's sales. The market had been developed by the competition existing between Frisby and Pinky.

In 2009 Kokoriko had $49 million in sales;[24] Frisby had $42 million and La Brasa Roja $35 million.[25] They also competed with informal competitors in the market who were attracted by the low cost of chicken (15-20% less than beef) and high per capita consumption.

Kokoriko

Kokoriko was founded in Bogota in 1969 under the name Colonias. In 1975 it launched its restaurants using the name Kokoriko; the first one was located in Cali. Originally, Kokoriko only sold fire-roasted chicken with local side dishes, such as sweet plantains, arepas and others. In the 1980s they diversified their products and implemented new technologies. They also focused on food development and quality processes.

At the end of the 80s and beginning of the 90s, they started building a new production plant that was capable of processing greater volume to cover existing demand and also process other products besides the traditional roasted chicken, such as breaded, fried and frozen chicken. The plant was equipped with the latest production and refrigeration equipment that used European and North American technologies. At first non-traditional products were sold to institutions: supermarkets, schools and clubs, to be prepared instantly.

[24] The representative exchange rate was 2,044.23 Colombian peso per United States dollar on December 31, 2009. Banco Central de Colombia, http://www.banrep.gov.co/es/trm.

[25] Source: Turbulencia empresarial en Colombia: sector restaurantes comidas rápidas: Kokoriko, Frisby y la brasa Roja / Juan Pablo Roa Martínez [et al.].— Centro de Estudios Empresariales para la Perdurabilidad – CEEP, Facultad de Administración, Universidad Colegio Mayor de Nuestra Señora del Rosario. Bogotá: Editorial Universidad del Rosario, 2011:

In the mid-1990s the company made a change in one area to reach clients: home delivery. To place an order for delivery customers had to contact the restaurant closest to their location and that restaurant filled the order. In 1994 Kokoriko inaugurated a centralized call center service that allowed clients to contact a single phone number and the system sent the order to the nearest restaurant depending on the location. This change was made to improve customer service.

Kokoriko was one of the first fast food restaurants to become ISO 9001:2000 certified. In 2006, because of its standardized processes, it was able to enter the United States market with its first restaurant in Miami. The decision to open in Miami was based on the presence of a large number of Colombians living there.

In 2007[26] Kokoriko launched a new, more exclusive, restaurant. Kokoriko Boutique was highly trafficked and offered a gourmet menu, which included products, such as Filet Mignon, cocktails and ice cream with special combinations.

In 2009 Kokoriko had wide coverage and close to 100 restaurants with sit-down dining, self-service and Kokoriko Boutique options in Colombia's largest cities: Bogota, Girardot, Valledupar, Barranquilla, Villavicencio, Neiva, Ibague, Bucaramanga, Cucuta, Melgar, Santa Marta and Cartagena, along with Miami (see Exhibit 9).

As part of its distribution channels, Kokoriko offered home delivery through a centralized call center, online orders for home delivery, restaurants at shopping centers, window restaurants and stand-alone restaurants.[27]

La Brasa Roja

La *Brasa Roja* was founded in Bogota in 1980 with a small restaurant in the Kenedy neighborhood. Its first restaurant outside of Bogota opened in 1990 in Cali after the Bogota market became stable. In 1986 the company changed its image for the first time, improving its restaurants and making them more user-friendly. Their menu selection centered around roasted chicken with traditional side dishes, such as arepas, plantains and French fries. In 1998 the company changed its image again and kept it until 2007, when it made its final change and architectural improvements to align better with changing customer preferences.

La *Brasa Roja* expanded to Medellin in 2008, opening its first restaurant near the Lleras y Laureles Park, an area with high traffic. In 2009 La Brasa Roja's growth continued in Medellin, where they already had three restaurants. They opened an additional four restaurants in Bogota. At the end of 2009, they had 39 restaurants in different cities.

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[26] Source: http://www.portafolio.co/archivo/documento/MAM-2593191
[27] Stand-alone restaurants offer their own parking and are generally located on their own properties in high trafficked areas.

La *Brasa Roja* offered two categories of products: roasted chicken and fried, breaded chicken and appetizers. La Brasa Roja offered traditional and alternative menus, making it similar to Kokoriko. The traditional menu had roasted and fried chicken. Its alternative menu included appetizers (fried plantains, arepas, and chicken wings), soup (ajiaco), entrees (chicken breast), meat (sirloin), fish and rice (salmon and rice with chicken), hamburgers, salads and desserts.

La *Brasa Roja* had restaurants in three important cities in the fast food market: Cali, Bogota and Medellin. Restaurants provided delivery and sit-down dining options, as well as a varied menu.

Exhibit 10 shows a comparison of the main chicken fast food restaurant competitors by area. Several factors that impacted competition and were relevant to clients in 2009 were: price, quality, product innovation, packaging, amount of technology applied by the company, customer service, healthy food options and growth in sales.

Pinky

Pollo Frito Pinky was founded in Medellin in 1987 as a result of a dispute between Frisby and its franchise. Frisby entered Medellin as a franchise with its first restaurant opened by a family friend. The franchise was responsible for investing in required equipment, the property and directly hiring all human resources needed. Frisby had the responsibility of transferring its knowledge, known as the Frisby System, supporting the selection of the property and training the franchise employees in operational issues, company culture and managing the restaurant. In addition, Frisby provided brand support and quality control. The franchise agreement limited operations to the city of Medellin.

The restaurant was a success in its first year of operations. They decided to grow through franchises and their own restaurants in the city. During the first year of operations, Frisby opened six franchise restaurants. In the first two years of the franchise agreement, Frisby and its franchise owners began having problems, leading to the termination of the contract. At that point the franchise owners created a new company, and the Frisby restaurants that they owned at that time were rebranded as Pinky. The Pinky restaurants were remodeled and opened under the new brand name; however, they generally did not differ much from Frisby's restaurant design. The menu was based on fried, breaded chicken and had products similar to Frisby's. Both Frisby and Pinky grew rapidly in Medellin.

In 1988 Frisby sued Pinky for unfair competition because in 1987 Pinky had published an ad in the *El Colombiano* newspaper saying "Frisby has changed its name here to Pinky." That same month the *Patria de Manizales* newspaper published that "FRISBY WILL CHANGE ITS NAME: Beginning November 15 the Pollo Frito Frisby company will legally dissolve and become Pollo Frito Pinky." This situation created confusion in the market about the brands.

While the lawsuit was processed both companies were ordered to continue regular operations. In 1996 Pinky only operated in Medellin with 11 restaurants around the city (see Exhibit 11). Six of these restaurants had been selected and approved by Frisby. Window stands accounted for 60% of the restaurants; 30% were located in the street and 10% were stand-alone establishments. These restaurants were located in highly trafficked areas visited by Colombia's 3rd, 4th, and 5th segments. Pinky had the equipment, know-how and quality standards of the Frisby System, since they had been provided by Frisby. The Pinky brand was well-positioned among consumers in Medellin in 1997 (see Exhibit 12).

As a result of the fierce competition and popularity of fried chicken in Medellin, the market grew considerably, and Pinky became the city's most important competitor. The major damage that Pinky had caused was brand confusion. The logos were quite similar and Pinky used the slogan "The same flavor as always" alluding that it was the company that had designed the original chicken recipe.

In 1996 Frisby's lawsuit went to trial in Medellin's 9th District Court; Pinky was sentenced to pay one hundred million Colombian pesos in compensation for unfair competition with Frisby. Alfredo commented:

"After almost eight years of litigation, we were able to create jurisprudence on unfair competition in Colombia successfully".

Pinky was forced to assume the costs of the trial, and the sentence was dictated by Colombia's legal system. This created liquidity problems; however, the restaurants' owners continued operations as normal. The situation reduced Pinky's investment capacity to maintain its fixed assets and innovate.

In 2000 Colombia approved fiscal reforms that reduced the Value Added Tax (VAT) to 15%. In general, companies were pleased with the reform. The law had a negative impact on tax collection, and therefore on the country's finances, which led to its later reversal and back taxes for companies. In 2002 officials determined that companies had to pay the amount due. This new fiscal obligation further endangered Pinky's financial situation to the point that it could not pay. The Business Supervisory Board intervened with the intention to sell the company to recover what was owed. Pinky was well-positioned in the Medellin market and had 17 restaurants.

Once it was for sale, Frisby indicated its interest in purchasing the company. It felt pressure to buy as the sale had the potential to create new competitors since the Business Supervisory Board wanted only to sell the company and several buyers had demonstrated interest.

Frisby was able to make great progress with the negotiation; it carried out a study to find out which of Pinky's restaurants overlapped with its current restaurants (see Exhibit 11). The negotiation was advancing well, and the purchase seemed imminent. They signed confidentiality agreements and accessed Pinky's financial information during the due diligence process.[28] Two days before signing the deal, they found a problem through the investigation. A union had been formed in Pinky. Frisby decided not to purchase the company.

The Business Supervisory Board continued with the liquidation process, and Pinky was bought by an aviculture company, Idecampo.[29] Idecampo attempted a process of forward vertical integration in the supply chain. Pinky's restaurants continued operating normally under its new management; however, it lost its market positioning in Medellin, and sales dropped considerably to about 50% of what Frisby was selling in its similar restaurants. Idecampo's management was not efficient, and they had little knowledge about the business; therefore, in 2009 they decided to sell Pinky. Idecampo was Frisby's supplier providing refrigerated chicken for processing. Idecampo told them of their intention to sell based on a decision to refocus their core business to industrial chicken processing, since the company did not have the experience needed to manage restaurants nor the required customer service skills.

After learning about the opportunity, Frisby analyzed the situation and came up with three possible alternatives:

The first option was to not purchase Pinky. Frisby already had a good presence in Medellin with around 20 restaurants, and some of the company's managers thought that Pinky might go bankrupt given its current situation. Others thought that it was risky to not buy Pinky since Idecampo was going to sell and investment groups with experience managing restaurants had entered the fast food market recently. It was rumored that a group of foreign investors were interested in buying Pinky.

[28] Due diligence is a process carried out before a merger or acquisition of a company in which the investor evaluates the company's situation and potential risks of the transaction.
[29] Source: http://www.elcolombiano.com/BancoConocimiento/F/frisby_pico_primero_y_se_quedo_con_pinky/frisby_pico_primero_y_se_quedo_con_pinky.asp

The second option was to reinforce Frisby's presence in Medellin by opening new restaurants. At first thought they believed they could open four new restaurants in different parts of the city. Each restaurant would cost $213,000[30] to open, and it would take 4 months to train the personnel in operations and sales to reach average sales volumes (approximately $26,000 a month per restaurant).

The third option was to purchase the company. Idecampo offered to sell the 17 restaurants in Medellin. Some of them were located less than 100 meters from Frisby's. Restaurant infrastructure had deteriorated and needed remodeling. Pinky's sale price was five billion Colombia pesos. The remodeling and brand changes that needed to be made, however, would require an additional investment of six hundred million pesos.

The 17 restaurants generated sales of some 5.722 billion pesos in 2010,[31] which had been determined after doing a financial and operational study of the 17 restaurants and estimating income and operating costs for the first year of operations (see Exhibit 13).

In addition, they estimated possible growth that could be expected in the following years. On average, they expected 1.6% growth in volume, and they thought they could increase sales prices by up to 2% without affecting consumption. Likewise, Frisby's management team thought that the cost of living would increase by 3% in the coming years, so they could expect that same growth in the cost of raw materials and operations.

In addition to needing to conduct a financial analysis in which the profitability should exceed 15%, Francisco Guzman also was concerned about several issues:

1. The entrance of investment funds in Colombia could be a threat if investors purchased Pinky and developed it.

2. Purchasing Pinky could increase Frisby's debt to a level that would make the company's founders and management team uncomfortable.

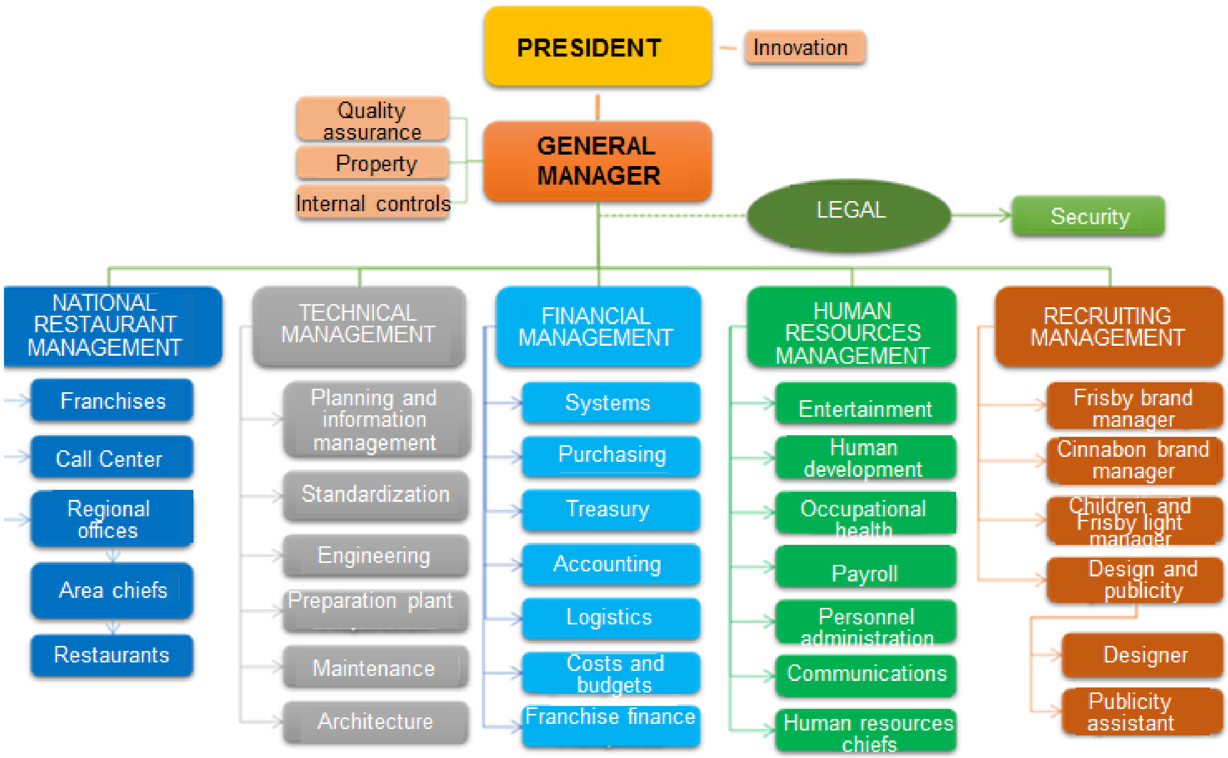
[30] Source: Baby, J, Frisby Mercadeo de comidas rápidas, EAFID Colombia 1998
[31] The representative exchange rate was 2,044.23 Colombian peso per United States dollar on December 31, 2009. Banco Central de Colombia, http://www.banrep.gov.co/es/trm.

Decision

The management team had to consider the decision carefully since their past experience could come back to haunt them: the purchase of Rico Mac Pollo, which had been traumatic to the company. When evaluating, they had to consider not only the financial situation that would normally be evaluated with a projected cash flow of 10 years, but also the strategic aspect of the purchase.

Exhibit 1

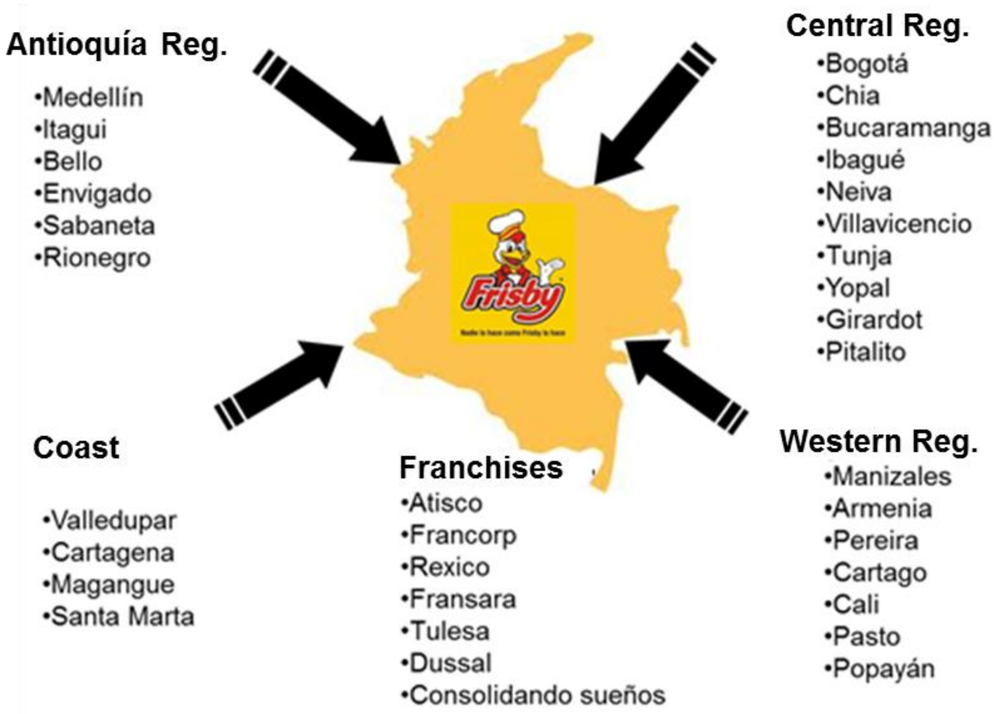
Frisby's Organizational Chart



Source: Pollo Frisby, 2014.

Exhibit 2

Internal Distribution by Region



Source: Pollo Frisby, 2014.

Exhibit 3

Description of the Main Activities Done to Develop Frisby's Human Resources

The four main activities that Frisby did as a central part of its company culture were: Suani, neurolinguistic programming, biodanza and ontological coaching.

Suani was a technique to improve self-awareness in people. It helped them heal from unresolved trauma and surround them with energy from their coworkers.

Another activity they began using was neurolinguistic programming (NLP). Neurolinguistics as a science was about modeling behavior and relationships based on oral and physical communication. NLP used mostly oral language to program behavior in a group of people and foster self-knowledge and self-awareness. In Frisby the practice was used to lead to behaviors that helped staff be more successful and perform more wholly.

Biodanza was another activity to improve communication among people. Biodanza was a system to develop self and knowledge that was created by Rolando Toro in the 70s. It was a human integration system32 for organic rejuvenation, improving emotion and relearning original life functions. It was mainly applied in communal settings with music, song, movements and group encounters. The purpose of the method was to develop human skills, feelings of happiness and communication skills and improve human relationships. The senior management participated in one-hour sessions at least once a week, which helped them improve their communication and relationships. Liliana had received training to become a biodanza instructor, as had her niece Gloria; both led the classes and helped their coworkers improve their performance. The classes were offered to both senior managers and staff at other levels. The Hoyos family farm, Sierra Morena, was used as a retreat to carry out biodanza workshops and training with personnel.

Coaching was another practice that was done frequently at the company. Liliana had become certified as an Ontological Coach and practiced it in the organization with potential candidates who received coaching sessions as part of their personal and professional development. Workshops to overcome fears and strengthen administrative skills, along with Suani, were offered as part of the staff's overall development.

[32] Source: http://biodanza.org/es/biodanza/definicion-de-biodanza, viewed May 2014

Exhibit 4

Activities Normally Carried Out as Part of Frisby's Business Culture[33]

Activity
Transactional analysis
Transcendental meditation
"Avance" human development workshops
Working inside: overcoming fear
Outdoor training workshops
Internal service and leadership
Developing teamwork
ARL (Action Reflection Learning)
Ontological coaching
Ocean workshop
Consolidating teams
Suani
Neurolinguistic programming
Leadership, communication, conflict management
Biodanza
Developing leadership
Developing awareness and sense of role
Administrative strengthening

Exhibit 5

Colombia's Economic Data[34]

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
GDP per capita (US$ current)	2503,5	2421,3	2376,1	2261,3	2752,9	3392,9	3712,8	4663,5	5405,1	5105,0
GDP per capita growth (% annual)	2,7	0,0	0,9	2,3	3,7	3,1	5,1	5,3	2,0	0,2
Net foreign direct investment flows (% GDP)	2,4	2,6	2,2	1,8	2,6	7,0	4,1	4,6	4,2	3,1

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[33] Source: Sustainability Report 2012, Frisby 2012.
[34] Source: Elaborated using data from World Data Bank:http://databank.worldbank.org/data/views/reports/tableview.aspx

Exhibit 6

Consumer Price Index[35]

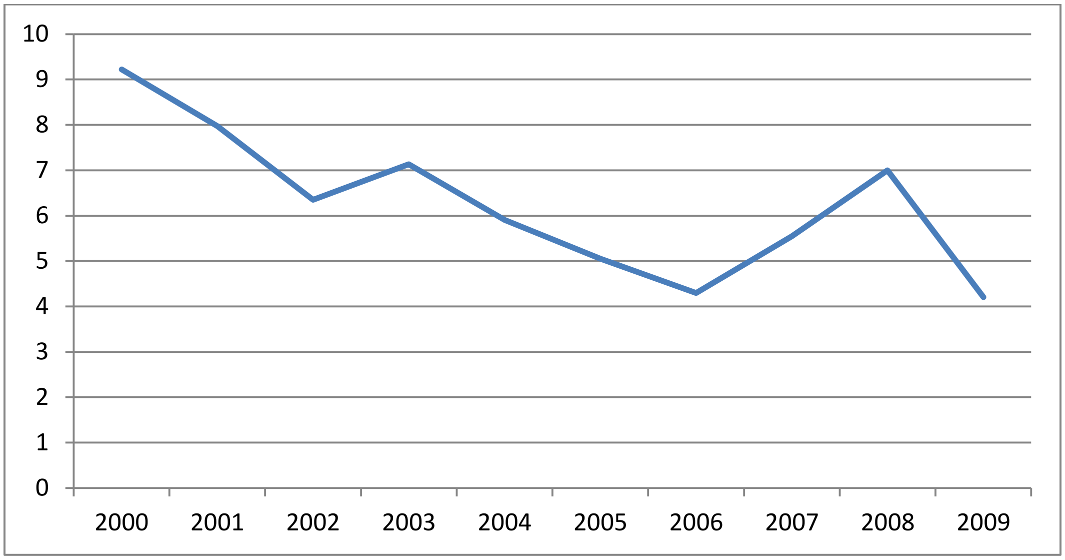
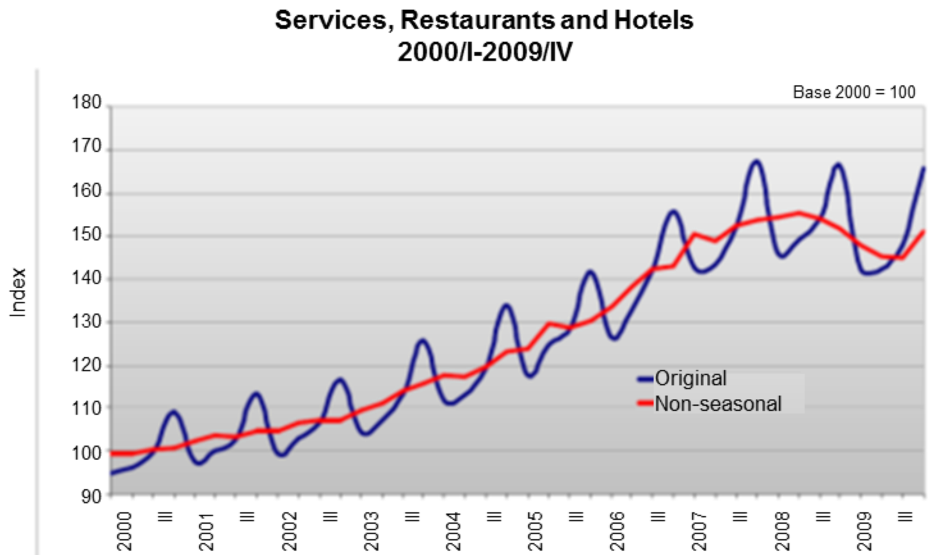


Exhibit 7

Behavior of Services, Restaurant and Hotel Sector [36]



[35] Source: Elaborated using data from World Data Bank http://databank.worldbank.org/data/views/reports/tableview.aspx
[36] Source: DANE Press Bulletin, "Producto Interno Bruto cuarto trimestre 2009", Statistical Administration Department.

Exhibit 8

Market Distribution of Restaurants by Geographic Location[37]

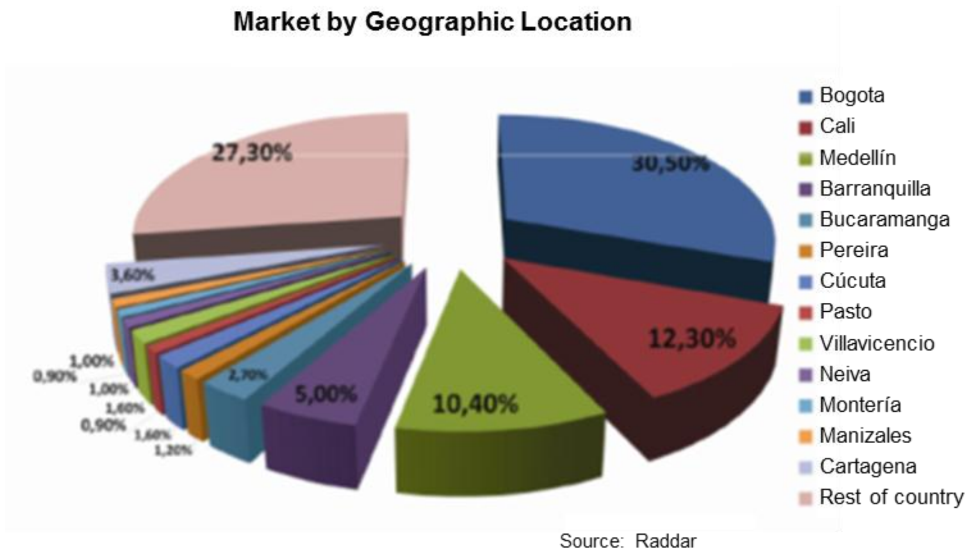


Exhibit 9

Map of Kokoriko Restaurants[38]

[37] Source: Presentation: El Sector de la Hospitalidad en Colombia, Consultora Raddar.
[38] Source: http://www.kokoriko.com.co/resttukokoriko.html

Exhibit 10

Chicken Fast Food Competitors' Profile[39]

Competition factor	Frisby	Kokoriko	La Brasa Roja
Price	Medium high	Medium high	Medium low
Quality	High	High	Medium
Innovation	High	High	Medium
New technology	Medium high	Medium high	Medium high
Service (attention)	High	High	Medium high
Healthy menus	Medium high	High	Medium
Growth in sales	Medium high	High	Medium high

Exhibit 11

Comparable Points of Sale for Frisby and its Direct Competitor in Medellin (1997) [40]

Frisby	Pinky
Visitación	Visitación
Envigado	Envigado
La Diez	Oviedo
Itaguí	Itaguí
Colombia	Cundinamarca
San Diego	San Diego
La Setenta	La Setenta
Terminal Sur	Terminal Sur
Candelaria	Carabobo
Éxito	Los Sauces
La Playa	Avenida Oriental

[39] Source: Baby, J, Frisby Mercadeo de comidas rápidas, EAFID Colombia 1998
[40] Source: Baby, J, Frisby Mercadeo de comidas rápidas, EAFID Colombia 1998

Exhibit 12

Chicken Restaurants That Consumers See and Remember the Most in Medellin (1997, in percentages)[41]

	Remember	Seen the Most
Kokoriko	85	41
Frisby	83	20
Pinky	82	24
Pollos Mario	53	5
Chicken Special	7	1
Kentucky F. Ch.	3	-
Pollo Express	-	1
Others	-	2
None	-	6

Exhibit 13

Results From the Financial Analysis of Pinky in 2010[42]

Operating expenses and income from new restaurants (millions of pesos)	
Income	5,721.8
Cost of sales	2.406.1
Operating expenses	2,296.0
Other labor costs	108
Other operating costs	148.8
Franchise income	67.7
Administrative Expenses	130
Franchise Licensee Fee income	524
Fifth Year Remodeling Expense	800

[41] Source: Baby, J, Frisby Mercadeo de comidas rápidas, EAFID Colombia 1998
[42] The representative exchange rate was 1,913.98 Colombian peso per United States dollar on December 31, 2010. Banco Central de Colombia, http://www.banrep.gov.co/es/trm.

No One Does It Like Frisby Does It

Teaching Note

Relevance

At the beginning of 2010 Francisco Guzman, Frisby's General Manager, sat with his management team to evaluate the possibility of purchasing a competitor in Medellin, called Pinky.

Frisby was a Colombian company founded by Alfredo Hoyos at the end of the 1970s that owned restaurants serving fried chicken in Colombia. It also owned the Cinnabon and Sarku Japan franchises. The Frisby brand was well-known and popular in the Colombian market and was equated with quality and good service. In 2010 the company had 130 restaurants across the country; however, 30% of its sales came from the city of Medellin.

Pinky was founded in 1988 as a result of the termination of Frisby's franchise contract; the termination had created major brand confusion between Frisby and Pinky. In 1997 Pinky had a large market share in Medellin with 11 restaurants. Due to a lawsuit filed against Pinky by Frisby, the company was fined in 1998 and began to have liquidity problems until it was taken over by the Business Supervisory Board.43 Later, after a change in management led to lost market positioning, the new owners decided to sell the company.

One of Francisco's main concerns was that, at the time of the sale, several investment funds were buying restaurant chains in Colombia since it was an attractive market. The market had become more competitive, and if one of those investor groups bought Pinky, they could make it into a fierce, solid competitor.

Target Audience

This case study is a discussion tool for advanced MBA and EMBA students and professionals. Depending on the professor's needs, different parts of the case can be highlighted and used in courses focusing on business strategy, corporate growth strategies and marketing.

[43] The Business Supervisory Board is a technical office through the Ministry of Trade, Industry and Tourism with legal status, administrative autonomy and its own budget, through which the President of the country inspects, oversees and controls businesses; it also carries out duties established by law related to other entities, companies and people. From: http://www.supersociedades.gov.co/superintendencia/quienes-somos/Paginas/default.aspx

Teaching Objectives

1. Analyze the option to buy the company from a financial, strategic and/or opportunity perspective.
2. Discuss brand positioning in an acquisition process in emerging markets.
3. Evaluate the strategic and cultural aspects of a company as key factors in an acquisition process.
4. Evaluate the possible risks of an acquisition process in emerging economies.

Teaching Strategy

The professor may highlight the possibility that any competitor could buy Pinky because of the timing during a period of positive growth in Colombia's restaurant industry. The market has proven to be attractive for foreign investors. The professor should also highlight that Pinky is located in Medellin, which is an important city to Frisby because it accounts for 30% of its sales.

Trends in the restaurant industry, investment funds, consumer preferences and competitors in Colombia must be analyzed. The professor should also emphasize the concentration of sales in Medellin and growth in the number of people who eat out as indicators of the sector's growth.

In addition, it is important for the professor to present a detailed analysis of the options Frisby faces, market conditions at the time and the financial analysis of the purchase.

Activities

1) What is the situation that Francisco Guzman faces at the time he is evaluating the management decision?
2) What is the key decision to be made by Francisco Guzman and his management team?
3) What is Frisby's strategic positioning? What is its organizational culture like?
4) Who are the relevant competitors in the market?
5) What is the situation of investment funds in Colombia at the time of the potential purchase?
6) What is Pinky's current position in the market? Legally? How does Pinky affect Frisby in Medellin?

Should Frisby buy Pinky? Is it profitable to buy it? What are the risks of the purchase, or non-purchase? How easy would it be to integrate these two companies if Pinky is purchased?

Research

The case was written using primary research, including personal interviews with the Hoyos family, Frisby owners and founders and the management team. It also included secondary research on relevant industry trends, Colombia's market characteristics and public data.

The case includes the company's history, a description of the competition and investment and market information. Frisby represents a unique way to do things organizationally since it has an HR department that contributes to the company's regular operations.

Financial Analysis

The instructor should ask the students to develop a ten year discounted cash flow analysis on the purchase option. Data to make the necessary calculations could be obtained from different paragraphs of the case, such as the following page 20:

"Pinky's sale price was five billion Colombia pesos. The remodeling and brand changes that needed to be made, however, would require an additional investment of six hundred million pesos"

"In addition, they estimated possible growth that could be expected in the following years. On average, they expected 1.6% growth in volume, and they thought they could increase sales prices by up to 2% without affecting consumption. Likewise, Frisby's management team thought that the cost of living would increase by 3% in the coming years, so they could expect that same growth in the cost of raw materials and operations. Page 21

In addition to needing to conduct a financial analysis in which the profitability should exceed 15%, Francisco Guzman also was concerned about several issues…" Page 21

From these paragraphs the following data can be extracted:

- Sales annual growth: 1.60%
- Price annual growth: 2%
- Cost of goods sold annual growth: 3%
- Expenses annual growth (Includes operational, labor, administrative, and other expenses): 3%
- WACC: 15% (project's cut rate)

Exhibit 13 from the case presents the detailed financial analysis for year 2010.

Based on this data the discounted cash flow can be constructed as presented in Exhibit 1. The project's expected internal rate of return is 15.6% which exceeds the cut rate, so the project is financially viable. The instructor should emphasize that there is no sensitivity analysis variations on the sale price and or volume might severely affect the IRR and make the project financially unviable.

Conclusions

The case may be used to illustrate different situations faced by a company deciding to acquire a competitor. It may also be useful to generate ideas and conclusions about topics, such as entrepreneurship and innovative human resources practices and their impact on the organization. The particular characteristics of Frisby's culture must be considered when discussing potential integration problems with Pinky if they finally decide to buy it.

Exhibit 1

Discounted cash flow analysis for purchase evaluation

	0	1	2	3	4	5	6	7	8	9	10
Revenue		5.721,8	5.929,7	6.145,0	6.368,2	6.599,5	6.839,2	7.087,6	7.345,0	7.611,8	7.888,3
Cost of sold Goods		(2.406,1)	(2.517,9)	(2.634,9)	(2.757,4)	(2.885,6)	(3.019,7)	(3.160,1)	(3.306,9)	(3.460,6)	(3.621,5)
Operational Expenses		(2.296,0)	(2.364,9)	(2.435,8)	(2.508,9)	(2.584,2)	(2.661,7)	(2.741,6)	(2.823,8)	(2.908,5)	(2.995,8)
Labor Expenses		(108,0)	(111,2)	(114,6)	(118,0)	(121,6)	(125,2)	(129,0)	(132,8)	(136,8)	(140,9)
Other Operational Expenses		(148,8)	(153,2)	(157,8)	(162,6)	(167,4)	(172,5)	(177,6)	(183,0)	(188,5)	(194,1)
Adminsitrative Expenses		(130,8)	(134,8)	(138,8)	(143,0)	(147,3)	(151,7)	(156,2)	(160,9)	(165,7)	(170,7)
Franchise generated revenue		67,7	69,8	71,9	74,0	76,2	78,5	80,9	83,3	85,8	88,4
Perpetuity											7.402,3
Purchasing Price	(5.000,0)										
Remodellung	(600,0)					(800,0)					
Franchise License Fee	524,5										
Flujo Neto	(5.075,5)	699,9	717,4	734,9	752,3	(30,3)	786,9	804,0	820,9	837,4	8.255,9

NPV	**$142,10**
IRR	**15,6%**

Source: Pollo Frisby, 2014.