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**Operational Review and Recommendations
For City of San Diego Golf Operations
In
San Diego, California**

EXECUTIVE SUMMARY

Prepared For:

City of San Diego
202 C Street, M.S. 7B
San Diego, CA 92101-4806

Prepared By:

**NGF
CONSULTING**

1150 South U.S. Highway One, Suite 401
Jupiter, Florida 33477
(561) 744-6006

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Executive Summary

The following is a summary of the significant findings and recommendations made by National Golf Foundation Consulting, Inc. (NGF Consulting). The supporting text and tables are found in the body of the attached report and appendices.

The City's golf facilities comprise a diverse mix of golf experiences. Both Torrey Pines and Balboa Park are rich in history, and Torrey is one of the most famous golf facilities in the world. Its long-time status as host of the San Diego Open and Buick Invitational, and its stunning oceanfront vistas, helped developed its reputation; the U.S. Open will surely cement its place forever as one of the premier facilities in the nation. Torrey Pines offers San Diego residents perhaps the best bargain in golf, and the popularity and reverence of the North and South courses among its patrons is unmatched among municipal golf courses nationwide. Balboa Park and Mission Bay offer additional, though less spectacular golf experiences, and provide San Diego residents and visitors with affordable alternatives to the San Diego market's generally highly priced public golf courses.

NGF Consulting's analysis has revealed a high-quality municipal golf operation that the residents of the City of San Diego can be proud of. Though our review revealed operational, administrative, and physical issues, at both the individual facility and overall administration levels, that need to be addressed to make the system even better, the San Diego system is one of the healthier municipal golf operations we've observed, and features one of the flagship municipal courses in the world.

The City's municipal golf operation is organized as an Enterprise Fund system, which means it operates like a business, with revenues expected to cover operational and maintenance expenses, capital improvement costs and any debt that may be incurred by the system. It is extremely important to maintain and manage the Enterprise Fund in a fiscally responsible manner so that the users of the facilities (golfers) are not only supporting the daily operational and maintenance costs, but also the long-term capital improvement projects to keep the courses competitive with the local golf market and up to today's industry standards. San Diego's system has been successful and self-sustaining over the years.

The City provides maintenance services and administrative support to each course, and also controls the pro shop and driving range at Mission Bay. Golf operations at both Balboa Park and Torrey Pines are leased out to private operators, though one of the prime considerations of this study is to determine whether it makes fiscal sense for the City to take back control of the golf shop at Balboa Park. Food & Beverage services are leased out to private operators at all the City golf courses.

For the past five years, the golf system has been operating under a Five Year Business Plan that was approved by the City Council in 2001 and expired in June of 2005. Since the plan was adopted in 2001, this division has assumed responsibility for the Mission Bay Golf Course and Practice Center in November of 2003, and the Torrey Pines Golf Complex was awarded the 2008 U.S. Open Golf Championship. In January 2006, a draft of a new five-year business plan was introduced outlining the plan for the Golf Division for fiscal years 2007 through 2011.

Having a formal business plan is very important in bringing consistency to the operation of the three golf complexes. The 2007-2011 Five-Year Business Plan is being used by the City to develop guidelines related to the Golf Division operation, institute a five-year golf course fee structure, organize a fair and equitable distribution of tee times for all players, and to outline a Five-Year Capital Improvement Program.

NGF Consulting has analyzed the City of San Diego municipal golf system, identified strengths and weaknesses, and made a series of findings and recommendations, at both the system-wide and facility levels, that are summarized below and detailed in the body of this report. We fully expect that the system will continue to be among the strongest in the country, and will likely improve further due to the expected improvements resulting from administrative and operational changes, as well as the capital improvements detailed in this study.

MARKET ENVIRONMENT

NGF Consulting investigated the basic demographic and economic variables that characterize the San Diego market, and summarized how these factors relate to the continued operation of the City's golf facilities. Specifically, we examined relevant characteristics of the local population, such as density, median age, and median household income levels. Age and Income figures should be considered in light of two important points: (1) In general, the propensity to play golf with greater frequency increases with age, making relatively older markets more attractive to golf facility operators, all other factors being equal; (2) Higher income residents are more likely to participate in golf, and they play more frequently than lower income golfers. NGF discovered that the population bases in the sub markets around the City's three municipal golf courses are diverse, with Torrey Pines market being by far the most conducive to high golf participation, Balboa's the least favorable, and Mission Bay in between.

A region's economy also has the potential to impact the performance of golf courses. In the early 1990's, San Diego suffered its greatest economic reversal since the Great Depression, a downturn that lasted from late 1989 through mid-1995, much longer than the overall U.S. recession. However, since that time the San Diego region has rebounded strongly. Much of the improvement has resulted from the emergence of a diverse economic base necessitated by defense contract reductions and corporate down-sizing, the passage of the North American Free Trade Agreement, and aided by the growing importance of the tourism industry, stimulated by the completion of the Convention Center. The region's growing prominence as a "new economy" locale, along with its high quality of life and climate, has made it more attractive for new business investment, both for entrepreneur relocations and for major firms' expansion sites.

Utilizing predictive models based on ongoing golf market research, NGF consulting has made basic estimates of the demand for golf in the San Diego market, and we have documented the supply of facilities that is available to service that demand. NGF Consulting determined that the subject market areas, with the exception of the Torrey Pines submarket, are classified as "inactive". This means that these local markets have a very high proportion (relative to the national benchmark) of households available to support each 18-holes of golf in the community, but that these households have an overall demographic profile that is consistent with relatively low demand for rounds of golf. The implication for the City of San Diego golf operations is that growth in rounds at Balboa Park and Mission Bay must be cultivated by player development programs, loyalty programs that increase frequency of play, and by increasing the percentage of non-resident play.

Torrey Pines falls in what we term an "Opportunity" market, representing relatively high rounds demanded from its population, and a relatively high number of households to support each existing golf facility. Intuitively, this means that an opportunity may exist for a golf course operator to satisfy some of the unmet demand for golf in this market, though Torrey Pines is already very close to its desired capacity.

COMPETITIVE GOLF MARKET/BENCHMARKING

Two of the primary objectives of this study are to identify any opportunities that may exist for the three City of San Diego municipal golf facilities to increase market share and revenues, and to compare the subject golf courses to other local, regional, and national golf courses for the purpose of benchmarking fees, activity levels, and policies. For each City of San Diego municipal golf facility, NGF Consulting has collected rounds played data, fee information, and other basic operational information from subsets of competitors and comparable facilities.

Because of the very high quality of the Torrey Pines golf courses, the tremendous bargain they represent to San Diego residents, the stunning oceanfront setting, and the national reputation and brand equity that Torrey Pines enjoys, local competition is not a key issue for the facility, but analyzing other golf courses provided some benchmarking measures by which to compare Torrey Pines. The following subsets of golf courses were profiled: (1) Local Municipal; (2) National Premier Municipal; (3) California Premier Oceanfront Daily Fee; and (4) San Diego County High-End Daily Fee.

Though it can be argued by some that one or more San Diego market golf facilities may feature a superior golf course to Torrey Pines, no market facility compares to Torrey when all factors - the very high quality of the Torrey Pines golf courses, the tremendous bargain they represent to San Diego residents, the stunning oceanfront setting, and the national reputation and brand equity that Torrey Pines enjoys - are considered.

Two of the main conclusions drawn from our analysis were that Torrey Pines is priced significantly 'under-market', especially for San Diego residents, and that these residents receive a much deeper discount, relative to the green fee charged to non-residents, than residents receive at other area and national municipal courses. Torrey Pines' pricing structure represents discounts ranging from 58% to 67%, depending on when play occurs, compared to corresponding market average discounts of between 19% and 23%.

Activity levels among municipal courses in this market are high, averaging about 80,000 rounds (excluding City of San Diego courses) per 18 holes. However, there has been a general downward trend in play over the last five to six years, mirroring a national trend. Torrey Pines is the most active club in this market in terms of overall facility play, though rounds have declined even at this premier facility. Compared to the market, Torrey draws a higher percentage of its overall play from City residents, compared to other local municipal courses, as well as some other premium national municipal courses.

Unlike Torrey Pines, Balboa Park is under considerable competitive pressure, especially for non-resident rounds due to a spate of higher quality golf courses that are similarly priced, but a cut above Balboa in quality. This situation is exacerbated by the fluid nature of fees in this market caused by discounting, player loyalty programs, and programs such as the JC Players Club and the Southern California Golfers Club. As a result, with the current pricing structure, the City will find it difficult to compete for the higher revenue non-resident rounds. Balboa Park's advantage over its competitors is its premier location near downtown San Diego, and its proximity to Interstate 5 and the Port area. Balboa Park has an even higher percentage of resident play than Torrey Pines, at about 85 to 90% of total rounds, meaning that there are not as many higher priced non-resident rounds available to subsidize significantly discounted resident play.

Mission Bay, benefits from an excellent and easily accessible location, nice views, and a lighted range and golf course (the only one in the area). In terms of alternative length golf facilities, there is little direct local competition for Mission Bay or the Balboa Park 9-hole course. Tecolote

Canyon, a quality course with a nice setting and a lighted driving range, sets up as the primary competitor for both City short courses, followed by National City, Lomas Santa Fe, and a host of other alternative length facilities that are too distant to be considered primary competitors.

Rates at Balboa and Mission Bay seem generally in line with the market, though the absence of a discount for a 9-hole replay results in an effective 18-hole rate that is well above market. Also, the 18-hole fees at Mission Bay are moderately higher than we observe at chief competitor Tecolote Canyon, and even more so considering this course's \$25 special, which includes 18 holes, cart, hot dog, and soda. These types of deals are especially appealing to junior, senior, and price sensitive golfers, which often make up the bulk of customers at alternative length courses.

OVERALL GOLF OPERATIONS SYSTEM

NGF Consulting has observed a very well run municipal golf system in San Diego. By all measures, the San Diego municipal golf system is one of the most financially successful in the nation with net operations revenues (before encumbrances and general fund payments) of over \$4.7 million in FY 2005. Recent administrative changes, including the creation of new high level staff positions, seem to have resulted in a more proactive approach to charting the future of the program. The proposed Five-Year Business Plan shows that the Golf Division is prepared to face challenges head on, and recognizes and strives to address the balance that must be struck between the needs of residents and various user groups, and the necessity of sustaining the system's economic viability in terms of funding operations and needed capital improvements in the face of spiraling costs.

San Diego's Golf Division faces unique challenges - access and usage issues at Torrey Pines, prioritizing the Capital Improvement Plan for all courses, a mightily struggling operation at Balboa Park, the challenge of bringing Mission Bay back to past glory after years of neglect – just to name a few. The Division is also charged with stewardship of one of the premier golf assets in the nation, and with ensuring that the coordination of the 2008 U.S. Open appears seamless to the hundreds of millions of viewers who will tune in worldwide those four days in June.

Recommendations

NGF Consulting has prepared a schedule of recommendations for the Golf Operations Division that are intended to apply to all facilities system-wide and the administration of the Division. While these recommendations cover a wide range of topics the basic issue is for the City to continue with the plan proposed by Division staff to streamline the fee structures in order to promote understanding and efficiency. Essentially, all fees are adjusted of the baseline resident 18-hole rate at each course (actual proposed fees are discussed and evaluated in each course section). Though NGF Consulting advocates this system, which is likely to result in more efficiency in setting fees and in the budgeting process, we believe that it must be evaluated annually for effectiveness, especially at Balboa Park where competitive pressures are more evident and the market more fluid in terms of rates. Other system-wide recommendations made by NGF Consulting involve enhanced marketing practices and taking steps to control rapidly inflating labor costs.

TORREY PINES GOLF COMPLEX

Torrey Pines represents one of the premier golf facilities in the nation, and it ranks among just a handful of the best municipal golf courses in the country. Certainly no San Diego market facility

compares to Torrey when all factors - the very high quality of the Torrey Pines golf courses, the tremendous bargain they represent to San Diego residents, the stunning oceanfront setting, and the national reputation and brand equity that Torrey Pines enjoys - are considered. World renowned for both the quality of its courses and its panoramic setting, Torrey Pines has been highly decorated over the years.

With the recognition and awareness of the facility at an all-time high, and activity levels at or near desired capacity levels, access to the course by the various user groups becomes a source of contention (many operators would argue this is a good problem to have). Ensuring the appropriate mix of public access has become a top priority for the City and the new management team of the Golf Operations Division. In the previous business plan, the City Council approved a distribution of rounds played at Torrey Pines be allocated 70% to residents and 30% to non-residents, ensuring that the resident public continues to have access to the courses, while also allowing visitors the opportunity to enjoy the experience of Torrey Pines.

The management team must work within this parameter, as well as the constraints of the system regarding the total amount of tee times, which is governed largely by the tee time intervals at each course (10 minutes South, 7 minutes North) and the total capacity, currently budgeted at 100,000 annual rounds on the North Course and 72,000 on the South. While more rounds are possible, and have been achieved in the past, activity levels beyond what has been budgeted will surely be detrimental to the condition of this world-class facility. The delicate balancing act of meeting various groups' demand for tee times, the revenue needs of the golf enterprise fund, and the condition of the golf courses, has been addressed by the Division in its new (2006-2010) business plan, as well as by NGF Consulting in this report.

Another primary objective of the Plan and this study has been to determine appropriate price points for the facility. As we explore in much detail in the 'Competitive Golf Market/ Benchmarking' section of this report, green fees, especially for residents (with purchase of i.d. card), have been below market at Torrey Pines for many years. City residents of San Diego receive a much deeper discount, relative to the green fee charged to non-residents, than residents receive at other area municipal courses.

This situation has resulted in very large amounts of lost revenue over the years, a conclusion that was also drawn by a previous consultant to the City in 2001. NGF Consulting believes that demand for golf at Torrey Pines will prove to be relatively inelastic within the price point parameters proposed by the City, at least through FY 2011 (barring unforeseen events such as further catastrophic terrorist attacks on our nation), and especially in light of the anticipated effects of the 2008 U.S. Open.

It is apparent that green fees at Torrey Pines needed to be raised not only to bring prices much closer to 'market', but also to keep up with spiraling operating costs, and to help fund needed capital improvements. Unlike some municipalities that operate their courses as part of the municipality's general fund, which means that any shortfall in revenue to cover costs is funded by taxes, San Diego operates its courses using the enterprise fund system, which obligates the golf course to generate all the revenue needed to pay all the costs associated with the golf operation. *It is not uncommon for some courses to charge less for a round of golf than the cost of producing a round (as is the case for resident rounds at Torrey Pines, and for all rounds at Balboa Park), because fees have been allowed to remain low.*

Aside from the key objective of maintaining affordable golf for the residents of San Diego, the primary goals of the proposed fee structure at Torrey Pines are to bring non-resident rates to market-justified levels. Additionally, the fee structure has been streamlined, with all rates

essentially benchmarked against the 18-hole weekday resident rate. Finally, an advance reservation fee has been proposed to capture revenues currently going to tee time reservation companies. It is hoped that these adjustments will help the City capture needed revenues that will sustain the operation in the face of spiraling costs, thus ensuring the preservation of this premier golf asset for current and future residents of San Diego.

Another key issue at Torrey Pines is the adequacy of its clubhouse. NGF Consulting has concluded that, aside from being aesthetically unpleasing, it is inefficient and not up to the standards of the golf course and the City of San Diego. Golf carts and driving range are handled through the pro shop, under the purview of the Torrey Pines Club Corporation, while payment of green fees goes through the City-employed starter at a different location. Additionally, check-in is on the second floor of the building, which is never the most efficient or convenient choice for a golf operation. Golfers paying for green fees, golf carts and practice balls should ideally be able to do this in one central location. Finally, the food and beverage service, controlled by another vendor, is in a third location, attached to the Lodge and completely separate from the clubhouse, which has no food service. This set up precludes running a seamless and efficient golf operation, as well as the ability to cross-sell in one location, a key to maximizing revenue.

The maintenance operation, facilities and resources at Torrey Pines are first rate. While all maintenance programs can be bettered, our review reveals that this is a well-tuned operation with few problems. Staff and management seem to take great pride in the courses, and appear willing to jump in and tackle any issue that arises.

Recommendations

NGF Consulting agrees with the City's proposal in its Capital Improvement Plan to replace the existing clubhouse with a more modern, efficient, an attractive building. However, we caution that this capital improvement should not be prioritized first if the justification is enhancing revenues, as the building will likely not pay for itself in terms of direct incremental revenues, at least not in the short term (especially since much of the incremental revenue would go to lessees). Aside from efficiency reasons, it is our feeling that Torrey Pines should have a clubhouse befitting its status, and the City must decide if a functioning building is worth replacing sooner rather than later, especially in light of the worldwide exposure Torrey Pines and the City will receive during the U.S. Open.

Other recommendations made for Torrey Pines include improved website and search engine strategies, capitalizing on the U.S. Open hype, increased direct selling and adding a system to allow the City to capture advance reservations at the facility.

The financial implications of these recommendations are that the Torrey Pines facility is expected to continue to operate with strong and growing profitability, and solid margins due to high activity and high green fees. The continued 70%/30% resident/non-resident rounds played mix remains the goal, and a more market appropriate fee schedule will allow the City to capitalize on the strong demand for golf at this facility and capture more revenue to fund the capital improvement program.

When all capital improvements, encumbrances and general fund payments are included the projection, the Torrey Pines facility will produce a generally stable increase to the Golf Enterprise Fund of about \$3,000,000+/- per year, with exceptions in years when large capital improvements are proposed, such as 2007 and 2014.

BALBOA PARK GOLF COURSE

The Balboa Park Golf Complex is a highly prized location with a significant historical asset. The design by William P. Bell, even though it has been altered from its classic era style, is still evident and worth preserving and restoring. Many of the remodeled holes resulted in positive changes to the routing of the course. It is clear that the golf course and infrastructure at Balboa Park are quite old and in need of capital upgrades and better on-going maintenance. Consequently, as the condition of the golf course suffers, this only seems to detract from fact that Balboa Park Golf Course is in a premier location and is definitely not meeting its full potential, as evidenced by declining rounds played levels and large annual operating losses.

At present, more than 145,000 rounds are played on the courses, with approximately 85% of those being local residents. However, because of the current poor to average condition of the course and support amenities, it is likely that short-term revenue growth at Balboa Park will have to come from increasing activity levels through lower fees (than proposed), and taking control of the pro shop revenue categories. Once sufficient improvement has been made to the course and amenities, the combination of higher fees and higher rounds may be achievable.

NGF Consulting considers the fee increases proposed for Balboa Park as part of the new Five-Year Business Plan to be aggressive, in light of the current condition and level of support amenities at Balboa, as well as the highly competitive nature of the golf market at this price point category. For instance, 18-hole resident green fees increase by \$4 in FY 2007, while weekend rates jump by \$9 – increases of 17.4% and 36%, respectively. Therefore, unlike at Torrey, where resident rates are vastly under-priced based on market demand, Balboa may be at risk of losing some resident rounds if golfers no longer perceive value.

More important, Balboa is not competitive for non-resident rounds when we take into account the considerable price pressure from golf facilities that are a tier or two above Balboa in quality. Additionally, many area golfers have access to discounted rates at these clubs because they are county or Southern California residents, or because they are JC Players Card holders, SCGC Card holders, or seniors. Increasing the amount of higher-revenue non-resident play is one of the keys to returning this facility to profitability, especially since the percentage of resident rounds, which currently produce revenue less than the cost of production, is so high.

Recommendations

NGF Consulting has prepared a list of recommendations that addresses the main issues discussed in this report, and created a prioritized list of needed capital improvements for Balboa Park. In summary, the recommendations for this facility center on upgrading the golf course and taking direct control of the carts, range and merchandise operations. If the City does not assume this control, then any improvements made at the facility are likely to end up benefiting the lessee at Balboa more than the City. The first priority should be to improve the driving range. The NGF Consulting team has recommended a large-scale investment in the range, and our estimates show that this investment will lead directly to increased revenues on the driving range. The City will only be in position to enjoy those revenue increases if the improvements are made AND the City takes over the range operation.

NGF Consulting has also recommended a scaling back of the new Balboa clubhouse plan that was presented to us during this study. The NGF plan would be for an open-air tournament pavilion to be constructed as soon as possible along with a thorough renovation of the existing clubhouse building.

The other key recommendation made for Balboa Park is for the City to scale back the projected green fee increases, especially for non-residents. The NGF Consulting thinking on this recommendation is that the City should strive to do everything possible to GROW ROUNDS ACTIVITY at the facility, rather than try to generate revenue from higher fees. The NGF Consulting spreadsheet shows enhanced green fee revenue from reducing fees and producing just a one percent (1%) increase in resident rounds and a five percent (5%) increase in non-resident rounds. The NGF Consulting cash flow projection shows that the recommended and assumed changes will bring the Balboa Park Golf Course to a level close to operational break-even (revenues less base expenses before CIP, general fund, encumbrance) by 2009.

When all capital improvements, encumbrances and general fund payments are included, the Balboa facility will generally off-set the gains made at Torrey Pines, with Golf Enterprise Fund reduction expected in every year through 2020. While the NGF Consulting recommendations will help to reduce the operations loss from an estimated \$568,000 in FY 2006 to amounts projected at under \$200,000 for Fys 2007- 2010, the continued rapid growth in expenses will more than outpace the revenue growth in the years beyond 2011. In the years when larger capital improvement projects are scheduled, such as 2007, 2010, 2011 and 2017, the Balboa operation will negatively impact the Golf Fund by upwards of \$4.0 million.

MISSION BAY GOLF COURSE & PRACTICE CENTER

Mission Bay has been City-owned parkland throughout its existence, but was operated for about 50 years by a contracted private entity until November 2003, when the City took over operations. The facility benefits from an excellent and easily accessible location, nice views, and a lighted range and golf course (the only one in the area). In terms of alternative length golf facilities, there is little direct local competition for Mission Bay, other than Tecolote Canyon. Mission Bay enjoyed a great reputation in days gone by, when visitors to San Diego regarded the facility as a great family destination. While it is still enjoyed by families and visitors, the facility has a tired and worn out feel. Efforts to improve the physical facilities and programming will go a long way toward restoring a quality golf experience at Mission Bay.

In order to retain golfers and increase the frequency of their play, as well as draw new golfers and some of those that have left, the price/value proposition that the facility presents must be improved. In other words, it would be putting the cart before the horse to sink much investment into marketing dollars until the recommended physical improvements detailed below are acted upon. Foremost among these would be to address serious safety issues, improve the driving range and irrigation system, and improve the clubhouse, including adding a full service food and beverage provider.

These improvements and others should make the golf course more appealing to a broader group of potential golf customers, particularly visitors and county residents living outside the immediate area. However, physical improvements will not be enough. *After the facility is improved*, the City must elevate the perceived image of the facility in the golfing public's mind.

With higher maintenance standards, the addition of better amenities, and the completion of other capital improvements detailed previously, Mission Bay, like Balboa, should be able to build rounds and revenues. The course could host golf events and attract small tournaments once the infrastructure is in place to support them. It could also enact some of the strategies we detailed in the Balboa Park section centered around drawing more visitor play and creating successful player development programs, which should be a perfect fit for a facility featuring a lighted short course and practice range, and located just a short drive up Interstate 5 from the downtown and Port areas. Finally, the demographic profile of the surrounding neighborhoods is projected to

become more favorable for increased golf participation in coming years, as the senior population grows as a percentage of the overall population.

Because of the inherent price sensitivity of its clientele, the price points established by nearby competitor Tecolote Canyon, and the sub par overall quality of the facility, meaningful revenue increases are not likely to come from fee increases. In fact, the marginal increases proposed as part of the Business Plan are likely all that the market will absorb without a decline in play if the facility remains in its present condition.

Recommendations

The most immediate recommendation for Mission Bay is the addition of much-needed food service. While the addition of the food/beverage cart concession is a short term band aid, the addition of full food and beverage service is likely to attract new golfers to the complex (or bring back some old ones who had left), and is necessary to satisfactorily meet customers' needs, and to bring the facility up to the City's standards.

The second key recommendation for Mission Bay involves a much-needed upgrade to the golf course facility for safety and maintenance reasons. Some of the conditions present at Mission Bay are not only limiting its appeal to consumers but also making maintenance of the facility more cumbersome. The antiquated irrigation system is a key example of this.

The results of NGF Consulting's preliminary cash flow projection shows that the Mission Bay Golf Center should be able to produce enough revenue to cover its basic costs, with only the encumbrances and capital improvements bringing the operation into the red. If the City can attract a vendor/lessee to upgrade the clubhouse facility and start generating some lease revenue for the City, this operation should be able to cover all costs in the long run. Further, the NGF Consulting projections have assumed very conservative growth in the driving range revenues that could be higher if the facility is actively promoted to the beginner segment through group lessons and golf schools.