bae urban economics

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Memorandum

To: Juliet Sinisterra, Project Manager, Riverfront Park, Spokane Parks & Recreation

From: Ron Golem, Principal, BAE

Date: July 3, 2014

Re: Refined initial review of Pavilion Event Center financial projections

Key Findings

This memorandum presents a refined set of findings from those in our June 4, 2014 memorandum for the Pavilion Event Center (Center), based upon review of additional information and revised project pro forma provided to BAE. The following key findings are based upon analysis of this additional information. The methodology and other considerations used to formulate these findings are described in the memorandum.

- Spokane Parks & Recreation envisions operation of a year-around event venue in Riverfront Park, with primary usage between May and October and a maximum capacity of 2,200 persons. The Pavilion would be operated on an enterprise basis, with a combination of permanent and seasonal Park staff and contractors responsible for all aspects of operations, including bookings, event production, concessions (food and beverage, and merchandise).
- At stabilization, in Year 3, the annual attendance at Pavilion events would be more than 78,000 persons from 43 events, including live music, other performances, special catered events, and facility rental. This is a very high level of usage from a relatively small event venue.
- Based on assumptions in the financial model, total annual revenues at stabilization in Year 3 would be approximately $4 million, with annual operating expenses $3.7 million, and net operating income approximately $320,000. The Pavilion would not be required to cover any of the costs of its estimated $9.3 million in capital improvements, leaving any surplus from operations available to cover other costs of Riverfront Park operations. To the extent that stabilized net operating income is below this figure the Park will require additional subsidy.
- As an enterprise activity, the City need to carefully manage operations to ensure that ticket revenues, concession sales, facility usage, and event-related expenses differ cover all expenses and generate a surplus. Sensitivity analysis was conducted for the three adverse outcomes that have the highest chance of occurring, in order to evaluate the impact on operating results compared to those assumed in the pro forma:
    - *Sales as a percent of capacity*. The model assumes in Year 3 that ticket sales for all events achieve 90 percent of capacity. At a level of 75 percent, still considered good for small, publicly owned venues, net operating income would be reduced by a loss of

approximately $75,000 per year. This would represent just under two percent of revenues, within typical budget variance for this type of facility and able to be offset by cost savings, so the finding should be considered equivalent to break-even.

  - *Fewer revenue-generating events*. The model assumes a total of 43 ticketed events and venue rentals per year. If the number of ticketed events and rentals were reduced by 8 per year (just under 20 percent), a level still considered good by many small venues, net operating income would decrease to break-even.
  - *Lower ticket prices*. Ticket prices are a function of the acts that are booked. Average ticket rates assumed in the model "Tier 1" and "Tier 2" events were lowered by $10 each and "Tier 3" by $5 ach. This reduction in ticket prices to a lower level would reduce net operating income to just over $200,000 per year.

- The most likely factor to affect operating results is lower than projected sales. Particularly for live music acts, while popular events will sell out, other events will not be as successful, making it difficult to average 90 percent sales across all events.
- The analysis highlights that to be successful and achieve the strong projected operating results, Parks and Recreation will need to obtain the proper expertise to operate the Pavilion, attract acts, and run an aggressive marketing program and pursue bookings, and carefully control expenses. Although Parks and Recreation's operating model and procedures were not evaluated, it should be considered likely that there may be a need for greater flexibility in Center (and Riverfront Park) operations than is the case at other park locations.
- Parks and Recreation will seek an event promoter and has had preliminary discussions to identify interested parties. No independent assessment has been made of the pool of potential promoters. Securing a promoter for a 13-act summer concert series would shift the responsibility for profit or loss from the events to the promoter, along with the operating costs (including staffing). Parks and Recreation likely receive a percentage of ticket sales and concession sales. Further analysis would be needed to determine the how Parks and Recreation receiving less revenues but incurring lower costs affects the overall pro forma.

Scope of the Review and Methodology

BAE Urban Economics (BAE), a national urban economics and development advisory services firm, was retained by Spokane Parks and Recreation to conduct an initial review (akin to a "peer review") of the Department's financial projection for operation of the Pavilion Event Center. BAE has extensive experience in urban park business planning and concessions, and has worked for the US National Park Service, and a range of State-level, regional, and local Parks agencies. BAE's experience includes advising other cities on amphitheater projects.

The new venue would be located within the historic Expo '74 US Pavilion in Riverfront Park. Renovations planned for Riverfront Park would include improvements to the Pavilion so it can function as an event center, including an overhead covering for weather protection (although it will not be a climate-controlled facility). The venue would operate year-around, but most events would be scheduled from May through October.

BAE's review of the Center's financial projections involved a thorough review of the two most recent iterations of the financial model, prepared on June 6, 2014. BAE interviewed City staff involved in preparation of the projections. BAE identified a limited set of similarly sized amphitheaters around the US, and reviewed their financial performance, usage, bookings, ticket prices, and governance model. This information, along with BAE's experience from similar previous assignments, was used to conduct the analysis and formulate findings.

Limiting Conditions

BAE's work represents a limited review of information provided to it. No market analysis was conducted by BAE, nor was market research for a new event venue available. Competition with other venues in the local market area, including future venues, may affect the viability of the Center. A range of assumptions, based upon Parks and Recreation operations, including staffing costs, staffing allocations, projections for increases in operating revenues and expenses, and other factors were not independently reviewed. The analysis did not include an organizational assessment or evaluation of the Department's capability to operate the Center as envisioned, including the capabilities of Riverfront Park staff who would have a portion of their duties assigned to the Center. BAE's work did not extend to formulation or evaluation of alternative operating models, or development of a business plan.

Considerations

The new Center's size is constrained by the historic US Pavilion structure, and the surrounding park setting. These combine to limit its capacity to a maximum of 2,200 for live music events, and more for other activities. For music events his is smaller than most publicly-owned outdoor amphitheaters, whose capacities tend to run between 3,000 to 7,000 persons and include a mix of seated and lawn areas. The smaller size of the venue affects the touring acts it can draw, and the ticket prices that can be charged. The most likely mix of musical acts will be national artists either in the early or late stages of their careers, supplemented by local and regional artists (e.g. the Spokane Symphony). There are also opportunities to attract a range of other performances, including summer theater, and non-profit performing arts groups. The Center will also provide a venue for private events.

Parks and Recreation plans to operate the Center, serving as the event producer responsible for booking acts, marketing and ticket sales, and venue operation, including food and beverage and merchandise sales. This will be accomplished with a permanent Parks and Recreation staff at Riverfront Park, who will have a portion of their time allocated to the Center. This permanent staffing represents, including payroll taxes and benefits, will be $630,000 per year. Temporary seasonal labor will be used to support concessions and operations, at a cost, including payroll taxes and benefits, of just over $172,000 per year. Contract services related to event set-up and tear-down and event production will be used, for a total of $200,000 per year. This represents a total of $872,000 in annual fixed and variable costs for staffing; there is an additional $50,000 in fixed annual costs for utilities, repairs, and contract services for the facility. The remaining $2.6 million of operating expenses at stabilization in Year 3 consists of variable costs tied to events, including fees to entertainers, promotion and marketing costs, cost of goods sold, etc.

Parks and Recreation plans to directly operate the Center, although it is currently evaluating the option of entering into an arrangement with a promoter for the summer concert series. The availability of other Riverfront Park staff, including those with concessions experience, provides a straightforward way of folding the Center into the overall operation of the Park. However, doing so creates significant fixed costs, which in turn create a need for a high level of sales to fully recover those costs. Parks and Recreation's operating model also builds in assumptions that are unique to public operations, such as long-term costs increasing at a faster rate then revenues, which leads to a projection of break-even operating results for the Center by Year 12. A high level of ticket sales and facility utilization is needed for the Center to achieve the projected results.

There are alternative approaches that could be considered which use a smaller overall level of staff that is dedicated to the Center and employed on more of a seasonal basis, who would book acts and produce events, and operate the Center. A concessioner could take on the profit or loss operation of food, beverage, and merchandising, in return for payment of a percentage of receipts to Parks and Recreation. However, such an approach could support a lower level of overall staffing for Riverside Park. Further work would be required to determine the viability of this or other alternatives.

Another way to expand the Center's revenue base would be to broaden the number and types of activities. This would involve attracting a larger number of community-oriented performing arts groups, as well as holding other events such as movie screenings, festivals, and other activities. While these events may not generate nearly as much in ticket sales or facility rental revenues, the attendance they attract will generate revenues for concessions and achieve higher utilization and exposure for the Center.

Finally, a couple items were identified for further consideration by Parks and Recreation:

- Corporate sponsorships are assumed on a per event basis. There may be potential to generate greater revenues from granting naming rights for the entire Center. Other smaller cities have been able to generate $50,000 to $75,000 per year or more for naming rights.
- Revenue from pay parking, if the local market will support parking charges for events, is another revenue source. If this is a possibility, parking revenues generated from Center events should be shown in the Center budget.

Revenue Sensitivity Analysis

The financial projections for the Center envision a high level of ticketed events, ticket prices, and ticket sales. Further market analysis is needed to draw definitive conclusions on the ability to achieve these numbers. It is assumed that with proper marketing by adequate staff with the right qualifications, the projected figures can be realized.

As with any enterprise activity, operating results can differ from projections due to market or other economic factors or changes in circumstances. These can include competition from other venues (existing and future new ones) and changes in the concert industry. Sensitivity analysis was conducted In order to illustrate the potential impact that changes in certain variables might have on the projected operating results, focused on capacity and utilization, the number of events, and lower average ticket prices. To perform the analysis, all other assumptions were held constant, and one set of variables in the Parks and Recreation financial model was changed to highlight its impact upon total revenues and net operating income (variable expenses were lowered by the model as revenue decreased, however fixed expenses for labor remained the same).

The following scenarios were evaluated:

- *Sales as a percent of capacity*. The model assumes in Year 3 that ticket sales for all events achieve 90 percent of capacity. At a level of 75 percent, still considered good for small, publicly owned venues, net operating income would be reduced by a loss of approximately $75,000 per year. This would represent just under two percent of revenues, within typical budget variance for this type of facility and able to be offset by cost savings, so the finding should be considered equivalent to break-even.
- *Fewer revenue-generating events*. The model assumes a total of 43 ticketed events and venue rentals per year. If the number of ticketed events and rentals were reduced by 8 per year (just under 20 percent), a level still considered good by many small venues, net operating income would decrease to break-even..
- *Lower ticket prices*. Ticket prices are a function of the acts that are booked. Average ticket rates assumed in the model “Tier 1” and “Tier 2” events were lowered by $10 each and “Tier 3” by $5 ach. This reduction in ticket prices to a lower level would reduce net operating income to just over $200,000 per year.

It is unlikely that all three of the above scenarios would occur at the same time. If more than one factor should adversely affect Center operations, particularly the number of events, a corresponding reduction in the $2.6 million in annual operating costs could help offset a decrease in revenues. This analysis highlights the importance of the successful execution of a business plan for the Center in order to achieve the projected $320,000 in annual net operating income.

Conclusions and Potential Next Steps

This initial review of Center financial projections has highlighted that the unique circumstances of the Center and Riverfront Park mean that Parks and Recreation will need to incur substantial fixed costs and generate significant revenues in order to achieve projected results. A market study should be conducted to validate the reasonableness of utilization, ticket sales, and ticket prices. Development of a business plan for the Center will be important to identify the strategies and resources that will be needed for a successful operation.