So, You Think Your Business Is Profitable?

2018 Annual Conference

December 5, 2018

Topics of Discussion

- Trends effecting Outdoor Recreation Companies (ORCs)
- Why are we in business →What is Your Strategy?
- A little "Accountingneese"
- Marginal Contribution
- Cost Management
- Pricing
- Q & A

What is the Trend?

- Changing of competitor mix inside and outside of your offerings
- Core cost areas really on the rise, e.g., fuel, equipment, hay, horses, personnel costs, etc.
- Finding and retaining people back to the pre-recession days
- Very steady metamorphism of consumer tastes, expectations and behaviors

What is the Trend?

- Number of ORCs for sale in most markets is very high
- Nature of consumer outdoor recreation consumption continues to be stressed, where will it be in 10 years?
- Average age of owner/outfitter/operator of recreation businesses continues to rise, very little new generation recruitment
- Time to market an outfit averaging in excess of 2 years, some have been on market nearly 5 years

What is the Trend?

- Technology impacts on marketing and sales is profound, the pace and complexity continues to be overwhelming. Some EXPENSIVE developments:
  - Constant new search algorithms changing the SEO game
  - Social Media becoming more important then your site
  - All site platforms that aren't 100% mobile friendly are deemed user unfriendly to 58% of search market
  - Advisory site rating and reviews carry the vast majority of provider selection decisions

What’s a ORC To Do?

What is Your Strategy?

Begin with the end in mind:

- Survive the impact of trends
- Stabilize and coast
- Build Value
- Hobby or Lifestyle
- Exit

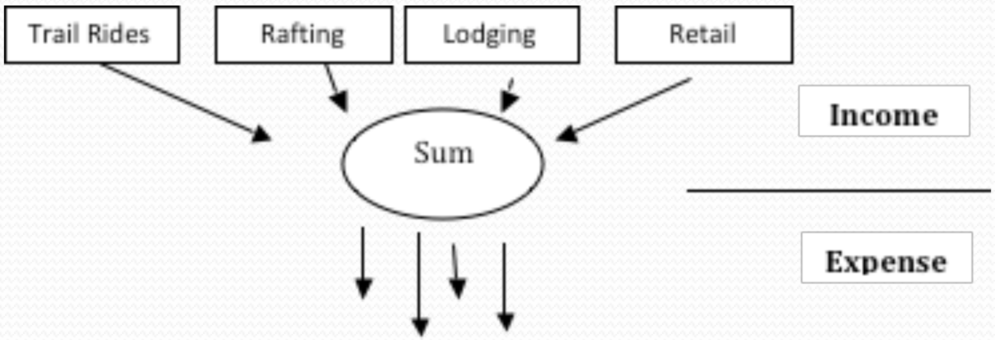
Strategy should drive your financial decisions

Accounting for ORCs

- There are three types of accounting
  - Financial – for the basic purpose of recordkeeping and statements and reporting to 3rd parties
  - Management – take the numbers and re-organize it so you can truly comprehend your business
  - Tax – specific techniques to manage tax implications of your business
- Too many ORCs emphasize financial or tax and ignore management

Accounting for ORCs

By its very nature, accounting looks backwards (never forward). The problem is that most organizations take so long to pull that information together and end up making decisions about the future without knowing how they've done in the past



Accounting is not cash flow, it is accounting for transactions. The management of cash flow is a whole different area (finance or treasury)

Accounting for ORCs

- Management Accounting. Utilizing accounting information in schedules, formats and statements that assist managers and owners in making better decisions based on the financial information and associated details
    - Marginal contribution is a core principle of management accounting – match specific expenses to specific revenue line items to understand how each product line is actually doing

Profit?

- Revenue minus cost. The amount one makes on a transaction.
- A company's total revenue less its operating expenses, interest paid, depreciation, and taxes. For example, suppose a widget manufacturer earns $1,000,000 in total revenue. The widgets cost $200,000 to make and his administrative and payroll expenses total $250,000. He also must subtract $50,000 in depreciation on his widget manufacturing equipment and pay $200,000 in taxes. His net income (OR PROFIT) is stated as: $1,000,000 - $200,000 - $250,000 - $50,000 - $200,000 = $300,000.

What do we know about costs?

- Seemingly always go up, rarely go down
- Rate of increase usually greater then what market will allow for price increases
- Most small businesses understand direct costs, e.g., food on a trip, payroll, but fail to account for indirect costs, e.g., depreciation, administrative, allocable.
- No one manages costs in a business like an owner, employees do little to control them unless you insist
- Too often, outfitters go for “easy” versus cost effective

A TRUE calculation of costs

- Try to break everything down by a unit such as a day of rafting or of an extended trip
- First account for all direct costs: labor, meals, regulatory, transportation, cost of assigned horse (this has many components, but need to calculate overall cost per horse, then by trips, then by day)
- Second apply burden of all indirect costs: depreciation, allocable portions of G&A, marketing, taxes, etc.
- Then sum up all elements making sure you have broken down to a per day unit of measurement

Where does ORC lack of profit mindset usually lead to?

Marginal Profit vs. Contribution

- The best thing you can do is break everything down to a per person/ per day cost
  - Example: summer trip = $275 per person per day. Summer trips last from June 1 to September 1 and you can isolate the amount of horses, shoes, employees, food, etc. that you use during that timeframe and break out the per person cost per day (total of expenses divided by the number of days – and then you can take it one step further and divide it by the number of guests). Set a goal such as 50% marginal profit per service line
- Another important element of management accounting is drilling down to a meaningful level of detail in each of your financial statements such that you can really tell how different service lines are doing and make good sound management decisions off of facts instead of judgments →Marginal Contribution

Marginal Contribution

	Trail	Raft	Retail	Lodge	Total
Revenue	10	100	30	10	150
Expense	1	50	20	1	72
Profit	9	50	10	9	78
Marginal Contribution	9/78 = **11.5%**	50/78 = **64%**	10/78 = **12.8%**	9/78= **11.5%**	78/78 = **100%**

- First glance computations can always be misleading
- Service lines can be profitable but insignificant based on overall contribution to company's profit
- Is a service line's gross profit dependent on volume?
- How much capital goes into the development maintenance of a service line?

Marginal Gross Profit

How do you compare? Best in Class GP% by Service Category:

Rafting = 60%

Hunting = 70%

Trailride = 75%

Lodging, Dude/Guest Ranch = 45%

Guided Multi-Night Trips = 55%

Hunting = 65%

Touring = 80%

Marginal Gross Profit

Interactive Template Demonstration

Improving Performance

- Really only two things you can do:
  - Cut Expenses and manage costs appropriately
  - Increase Prices

Cost Management

- Set policy regarding costs: If → a cost doesn't increase profit, enhance service that should lead to price increase, or add needed risk management protections Then → don't incur it!
- Go line item by line item and ask, if we cut this expense, what will be the impact?
- Know the profit impact of your "discretionary expenses" and recalculate profit without
- See 50 ways to cut expenses

Pricing Strategy

- Your pricing has to match your company strategy
- You absolutely need to know what your industry and competitors are doing
- Pricing should be visited often and adjusted annually
- Do your homework!

What is the Competition doing?

- Analyze every outfitter listing services in your area that has a website for the first 20 pages on organic listing
- Come up with different outfitter businesses noting offerings, prices and competitive advantages
- Recorded on spreadsheet:
  - Price per trip & number of days
  - Calculated average price per trip day
  - Repeat on spreadsheet for as many lines of service you have

What is the Competition doing?

- Example Results for Hunts in NW Montana:
  - Average price per hunt = $4,286
  - Average number of days = 8 days
  - Average price per hunt day = $630 per day
  - Highest and lowest = $829 & $286
  - Calculated average cost per hunt day (done by Pat as an educated guess) = $400

What will market bear?

- Are your longer term clients really your best if they won't let you raise prices?
- Keep an eye on market movement, not only what direct competition is doing but other trends in industry
- You can be the highest price if you add the most value
- You can only be the low price leader if in fact your costs are lower then everyone else
- Learn that slight increases annually at least keep pace with inflation.

Making the case for why increasing prices is right and just

- Is your intent charitable or are you trying to provide for your family and future?
- If you provide service, and deliver on your promise, then customers in fact do not mind paying, they expect to.
- Keep with in striking range of competitors, the lower you get the worst your reputation becomes, market thinks something is wrong

What Tactics Should We Employ?

- Generate Strategic Options
  - What are your options?
    - Consider all possible strategies
    - Narrow down to ones that make sense for you and others involved and where you are at in life
  - Which Options will help me survive and perhaps improve and sustain my ORC's position?
    - Can I change the game?
    - Can I chose my competitors/compliments?
    - Can I alter my relative position?

What Tactics Should We Employ?

- Test the Strategic Options
  - How will competitors, suppliers, complementors, customers respond?
  - Can negative impacts from regulatory change be frozen?
  - Are competitors threatened?
- Check For Sustainability
- Decide & Implement

Questions?

Thanks