

The Pros and Cons of Leasing

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One of the surprising findings of the 2004 Golf Club Survey, as detailed in the Australian Golf Industry Report – 2004 was the level of golf cart ownership evident around the country. The number itself wasn't the surprise (56% of clubs) nor the average carts per club (1.8 per every 100 members). It was how they are owned.

The table below, an example of the tables to be found in the 2004 report, identifies how these clubs own their carts, noting the percentage of clubs who chose to either own or lease golf carts. As the table reveals, there is actually a higher level of ownership lower down the annual fee scale vs that evident higher up the scale. One could assume, by simple fee positioning, that it is actually the clubs higher up the scale that could more easily afford to own carts (have the capital to spend) so what do these guys (actually only 10% to 30% more) know on balance that the others don't?

Annual Fee	% of Golf Carts Owned	% of Golf Carts Leased
<\$100	80%	20%
\$100 - \$249	83%	17%
\$250 - \$499	70%	30%
\$500 - \$999	55%	45%
\$1000 - \$1499	57%	43%
\$1500 - \$2000	42%	58%
\$2000 +	69%	31%
Average	69%	31%

Source: Australian Golf Industry Report – 2004

The aim of this article is therefore to take a closer look at the pros and cons of leasing. We have used the golf cart example above as that is something all industry people can identify with but the following discussion is equally applicable in other parts of the industry such as maintenance and clubhouse equipment. Now before we start and get drowned out with comments that leasing costs more than outright ownership, we accept that this argument is technically correct but in the current day where member satisfaction is high (or should be high) on all club priority lists, we want to point out that some qualitative counter arguments also exist which may actually offset this financial cost (not necessarily as high as you may think) incurred. It is our view that leasing should at least be being considered by more clubs, especially as club infrastructures are maturing and the number of projects required are increasing.

An economics lecturer once said, "If it appreciates in value you should buy it, if it depreciates in value then you should lease it. So what is leasing? It is the right to use something over a period of time with having (initial) ownership of the actual title, rather than paying in full and in advance for its future use. The belief is spending money in this manner frees up capital for use in other areas. In the days of member satisfaction, should the goal not be to do as much as you can with the funds available? Some areas of the operation have no choice but to incur capital costs (say a new path or a new tee) but in others, such as golf carts, leasing may be a more appropriate strategy.

This argument is largely centred around who stands to benefit from the capital spend? Is it all members? Does it improve the level of member satisfaction for all, or only a few. Say a new path, all golfers, be it cart users or walkers, need to use it and it now provides for a hazardless and much smoother journey to the next tee or to the fairway. You would think that everyone benefits from it and could conclude that it is capital thoughtfully spent.

Let's look at another example. (There are more numbers involved here but they are necessary to make the point.) Take a sample club of 600 members. This club buys 10 new carts, \$7,500 each, \$75k total. Average number of rounds per member per annum is 30, and 80% of rounds at the club are member rounds. 10% of rounds at the club are taken with a cart. Average cart occupancy is 1.5 people with these members being the consistent user group. Doing the math (trust us) results in 1200 club member cart occupants for the year. Divide that by the average number of rounds per year (30) and it shows only 7% or 40 members actually directly benefiting from this capital spend on carts. (We'll round this to 10% to account for occasional users.)

Queue the member satisfaction goal and it is likely not so great for the remaining 90% of members. In this example, the new path would be more beneficial. Answer – capital spend on path, lease the carts. Result – all members happier. Sure, if you change some of the assumptions, usage patterns etc, you may get a different result but the point of this example is to show that options, outcomes and impacts should always be considered when determining how you'll spend your capital budget.

The next argument for leasing is that one of the common mistakes made by golf clubs is the retention of equipment long past its useful economic life. (FYI, the AGCSA Turf Industry Census conducted in 2003 showed that in excess of 60% of machinery being used in Australian clubs is presently more than 5 years old.) Whilst not a direct expense saving in itself, one of the benefits of leasing (assuming a well managed lease program) is the reduction in maintenance and repair costs to old equipment. Excess repairs mean equipment downtime and possibly increased labour costs to get delayed jobs finished. By not continually putting funds to old equipment, leasing equipment can not only save associated repair expenses (and time) but also leave more funds in the capital budget for other uses.

The final Pro is the bigger bang for the buck theory. Whilst we aren't recommending that all clubs should load up with leased equipment, leasing does enable you to achieve more with your money than you might normally if following outright purchase as you are only covering the cost of the interest component over the period, not the principal. This is not for everyone though and takes a well planned strategy to execute and exit from successfully.

Now for the Con's.

The biggest con/counter argument against leasing is obviously its financial cost. The 'cost' of leasing is interest and it will appear as an expense on the profit and loss statement, therefore not necessarily improving profitability. (If you were paying tax this interest is deductible but if not (like most clubs) it hits the P&L.) Why incur an interest cost if you can afford not to? See the paragraphs above for that answer, but what are we talking about in cost terms here? How big really is it? Our enquiries suggest a 8% interest rate would be at the top end of the market but we'll run with for this example.

Ten carts, \$7,500 each, 8% interest, 4 year term. Annual interest cost of \$6,000, total cost of \$24k. \$24k is 32% of the total if bought outright. So what has the club got? – Full use of and fully maintained carts (be it for only 10% of membership,) the same as if they had of purchased, but importantly they still have \$51k available in the capital budget to spend elsewhere (to hopefully increase the satisfaction levels of the remaining 90% of members.)

In summary, it is the level of member satisfaction, both now and in the short to medium term, that you should look to when considering how you are going to spend your capital budget. Perhaps a simple way to look at it is to ask whether the level of member satisfaction could be increased by the percentage interest cost? Member satisfaction could well be the measure of the actual return on investment. Your view on this will likely dictate which strategy you will ultimately go with.