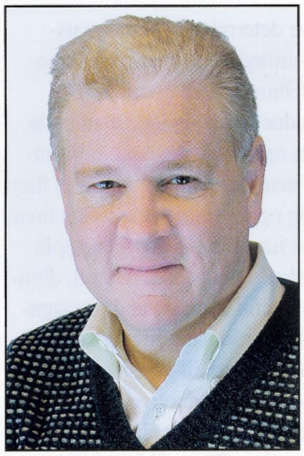

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Look for Opportunities When Times Are Tough

By GEORGE MCAULIFFE

At the recent ASI show in Las Vegas, we spent a lot of time in the aisles talking to operators, distributors and manufacturers. "How is your business doing?" was the opening question for many conversations, and the answers were mixed, although "soft" was a word we heard more often at this show than in recent years.

The newspapers are full of economic negatives, from gas prices to the credit crunch to housing, and general fears of a recession either here already or coming in the future. It's easy to wonder if the media is not helping to create a self-fulfilling prophecy.

I often drive between my offices in St. Louis and Kansas City. I haven't noticed a decline in cars or trucks on the road or waiting to gas up at the gas stations. A recent newspaper story was headlined, "Job Growth Drops Steeply." The article explained that job growth had dropped 0.6%, a little over half a percent, in the first quarter of the year. Not "steep" by my measure but to the overheated media trying to fill 24 hours on dozens of news outlets, it was a typical headline grabber.

Unfortunately, the negatives are what our customers see, hear and read, and it is clear that the procession of bad news flows from a national economic downturn, coming on the heels of a pretty prosperous period.

In boom years, too many of us tend to fly by the seat of our pants. High sales can forgive a lack of business discipline. The old cliché applies that "it's hard to think about draining the swamp when you're up to you're you-know-what in alligators." But this is now, and if now means a tougher business environment, good operators will take the time to truly analyze their company and determine what is working and what is not. This is an opportunity to carefully examine the economics of this business.

Managing expense control is part art and part science. Someone once said, "Any jackass can kick down a barn door, but it takes a carpenter to build one." Cost cutting by blunt instrument, without doing our homework, risks doing more harm than good. "Efficiency analysis" leading to expense savings is a virtue; "budget cuts" too often start a downward spiral. We can go seriously wrong if we cut past the fat and cut into the bone.

Revenues First

FECs are top-line businesses. Because we sell fun, most often in the form of time on games and attractions, much of our major costs are in our up-front investment. The lights have to be turned on every day, staff on post, rent and taxes paid and the bathrooms cleaned. In other words, many of our expenses are fixed. That's why the top line has the most to do with reaching an acceptable bottom line. The last sales dollar we collect is our most profitable dollar.

Is every revenue center in your operation producing profitability? Eliminating loss leaders (unless they are truly attracting audience) is a good start. At the same time, it is critical to strengthen the profitable revenue components.

When assessing a center in our consulting practice, we look at a combination of game and attraction performance factors: revenue by category (type, audience appeal, competitive profile), revenue per square foot and return on net asset value. Only after this careful assessment of our product mix do we begin to adjust it.

For example, if redemption games produce 60% of our game revenue but only represent 40% of our games, there is an opportunity to drive revenue by "right mixing." Another example might be the discovery that our children's rides (ages five through nine) have the highest revenue per seat in the FEC. Further examination shows that our children's game revenues rank high as well, but our proportion of parties from this age group ranks low. We have discovered opportunity via the mismatch of numbers. An examination of our party package construction and marketing may help us drive revenue to a market we're missing.

How about the quantity and quality of your marketing efforts? Most FECs are community based. Don't we have advantages to offer our customers if they are experiencing pressures on their household budgets? If gas prices are high, and our customers will stay closer to home this summer, it's a given that we market our facilities as a cheaper alternative to other entertainment and vacation options.

In tough times many retail businesses are cutting back, raising their prices directly or indirectly by giving their customers less. We have a tremendous opportunity here in the game and FEC business. Since much of what we do is selling time on fixed entertainment capacity, in many cases we can give our customers more fun for their money without reducing our profits. Again, careful analysis requires that we put our customer value proposition under a microscope, increase our value and, through marketing programs, make sure our customers know about it. Marketing short drive times and the fun to be had when they arrive, along with special offers, packages, "summer fun" programs, "value" party packages and the like, position FECs to appeal to expense-conscious consumers of entertainment.

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Using the Tools We Have

Many FECs are powered by debit card systems. I'm often amazed at how many use them only to collect revenues and churn out reports, but never unlock the value they provide in pricing flexibility via in-house marketing opportunities such as specials, package discounts, loyalty programs, bounce-back features and the like.

We really can't afford to pass on using all the tools at our disposal at any time but certainly not in a softer economy. We recently helped a client who had a terrific location just off an interstate ramp. Their sign package included a very exciting sign on the secondary road at the front of the building to capture the traffic coming off the exit but only a small sign with their name on the rear of the building, facing the interstate. It seems that was all the town would allow when they opened for business five years earlier. We suggested that five years later, with a great track record and reputation in the community, the city might be more amenable. Sure enough, they were; the tool of a free billboard was put to use and its value unlocked.

Take a look around, talk to your customers and your staff and hunt for ways to drive sales.

Redemption cost of sales is often seen as a variable expense, and it can be. Individual redemption games and the entire mix should be operating at a certain level of ticket payout. Each game has its own optimal level, and too high is as bad as too low. Again, many operators have the tools to manage the redemption process but don't establish the necessary "closed loop" system to control their redemption costs while driving sales. Rather than kicking down the barn door by carrying less merchandise (it's pretty well proven that proper displays drive sales), raising ticket prices or otherwise cutting too deep, operators need to understand the whole picture: game payouts, ticket value, price points and merchandise mix and a system in place to manage them.

Expense Control

We don't want to leave the impression that cost control is not important. In fact, it's essential. In the boom times, we tend to get sloppy, so most of us are overdue in "right sizing" our expenses. As above, careful analysis and a targeted approach is required.

Careful cost reduction can improve a business. We've conducted analysis through secret shopper visits that showed one of our client's night shift was overstaffed. We knew this because the employees consistently stood around talking with each other rather than paying attention to the customers. By reducing coverage we hit a double in that payroll was reduced while customer service actually improved.

Another FEC advertised on Saturday cable 12 months a year ever since opening five years earlier. After analyzing their audience, we determined (a) their customers had shifted away from the demographic watching Saturday cable; (b) between production and placement costs, this program represented a huge percentage of their marketing budget; and (c) they were missing opportunities to market their strengths. So here the facility hit a triple: reduced marketing expenses overall, elimination of wasteful expense and reassignment of dollars producing higher sales.

On the other hand, ill-considered cost cuts can be counterproductive. Across-the-board reductions are particularly bad ideas. We have seen the effect of blunt instrument cost-cutting in past recessions. Facilities that raised prices, cut marketing, reduced payroll, downsized restaurant portions, went to cheaper and less valuable redemption goods, deferred maintenance and fired their highest-paid employees soon saw a downward spiral in the business. Those that approached efficiencies strategically, with the master plan based on continuing to deliver a first-class entertainment experience for their guests, survived and prospered.

Hopefully, the current pressures on the economy will sort themselves out soon, but timing is always a big part of the unknown. In the meantime, as the man says, "it is what it is," and flying by the seat of our pants might well lead to crash and burn. The industry has been through this before. As an industry, we have the knowledge and tools to manage our way through it, if only we apply them.

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