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PART 1 OF 3

THOUGHTS FROM THE GOLF INDUSTRY SHOW

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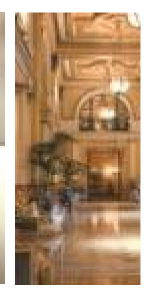


Thoughts from the Golf Industry Show

The following is the first in a three part series that examines the state of the Golf industry today. This first article explores the history and brings readers an understanding of issues challenging the industry, providing some context for readers. The second article explores the impacts to Golf Facility Financials and Value, while the third article looks to the future of the industry, and the issues that will shape its health moving forward.

Credit must be given to the large number of industry professionals at the show who were speakers, and whose thoughts, ideas and concerns I am liberally using. These insights are a direct result of their expertise and experience, and I would like to thank them for their input.

The Golf Development Cycle

Golf development has come full circle since from the beginning of golfs modern era, and it's insightful to understand the factors that led to the extensive growth in the game. The golf development cycle provides important context from which to look for clues to the future growth of the game. Looking back to understand the elements that contributed to the modern development era, a path for the industry to realize its full potential becomes clear. The early 1990's were the heyday for the golf industry, and the following were key facets of the industry at that time.

- The game of golf was growing in stature, and the future financial prospects for golf course operations looked extremely promising.
- Golf courses were one of the few government enterprises that could not only pay their operating expenses, but also pay their construction and development costs, and fund other activities as well.
- New resort and real estate developments, focused on golf, were being developed across the country, and resulted in the transformational evolution of course design, maintenance, and irrigation aspects of the game.
- Advances in club and ball technology were also changing the game, and requiring renovation and redesign of many of the existing golf courses.
- The baby boom generation had grown to the game of golf like none before it, and the aging of this demographic, and their substantial accumulated wealth looked to secure the future of the industry.
- The stars were aligned for the growth of the game and the development of golf courses.
- The National Golf Foundation initiated their now-infamous campaign to build a course a day during the 1990's in order to keep up with the projected demand from the baby boomer generation.
- The baby boomers would be reaching retirement age and would be at the peak of their golfing careers, causing a huge demand for tee times at courses across the country.
- The advent of the high-end daily fee golf course was redefining public golf. Pay-for-play golf courses with fees of $100 a round were springing up in metro areas across the country.
- As the expectations of the golfers grew, golfers sought an experience that was previously available only at private clubs or at exclusive resorts.
- Textron started a national golf course finance operation, the first of its kind within the industry, and provided a source of capital that had not previously existed.

- Golf course ownership companies were growing, and golf ownership was going institutional. Companies were acquiring and assimilating golf courses, and golf was being groomed to be legitimized as an asset class, just like office buildings, hotels, or apartments.

In 2013, it's clear that the future failed to live up to its billing for numerous reasons, but primarily due to the events of September 2001 as well as the great recession. The global financial crisis has rearranged everything from social constructs to financial realities, and the industry has given up so many of the gains that occurred during the past several decades.

There are however a few similarities of note between the state of the industry in the early 1990's, before the boom in golf occurred, and today.

- Capitalization rates for golf courses are now 12% and were then 12% as the push for growth began.
- There are no major national lenders providing capital to the industry.
- The number of golfers per 18 hole course was just below 1,800 in 1989 and has returned to approximately that same level today.

The major difference is that the industry outlook today is obviously more bearish in the near term, as excess supply continues to be present in the market, the capital markets remain difficult, and golf course distress is common. So while the 1990's were a dynamic and optimistic time for the golf industry, the future landscape of the business does not shine as brightly, but the market fundamentals are coming into focus, and better times are ahead.

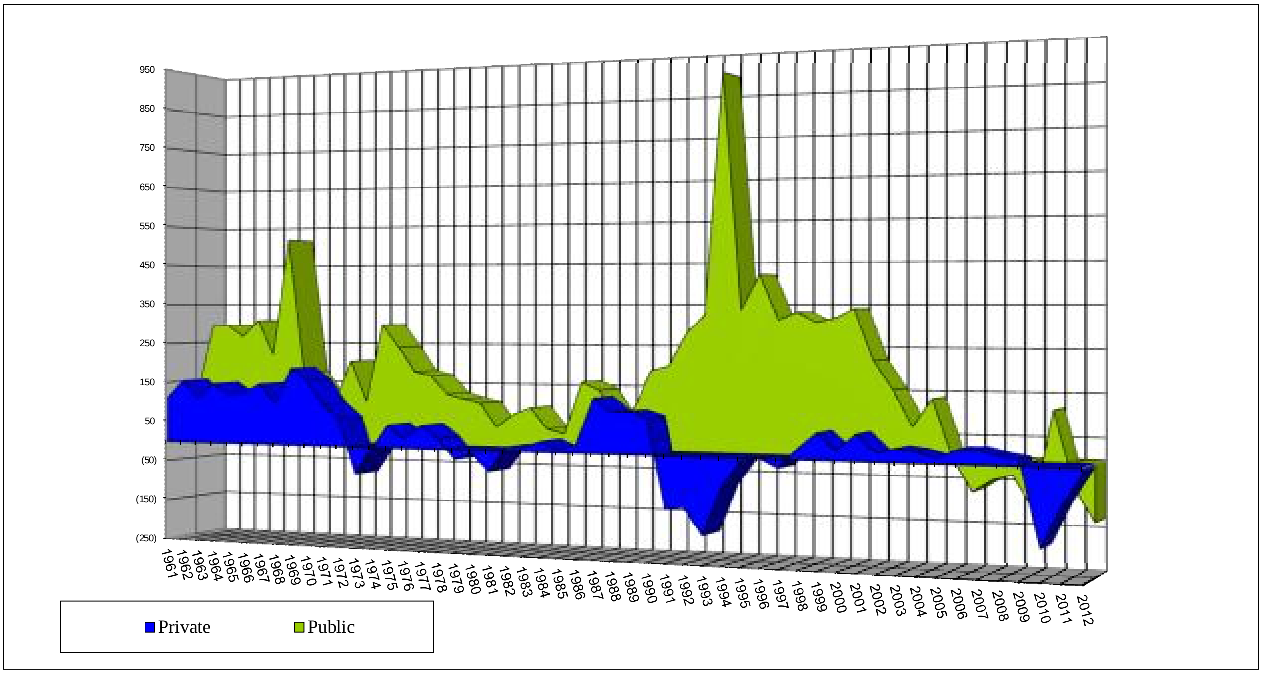
Trend Analysis and The Golf Development Cycle.

During the 20th Century, there have been three primary golf course development cycles, the first occurring in the 1930's, the second in the 1960's and the third in 1990's. Examining the change in golf holes over the past several decades, the thirty-year cycle is fairly clear. The characteristics of the latest cycle, in comparison to previous cycles, are described below.

- In the previous cycle, new golf hole additions peaked in 1968 and bottomed in 1985, representing a 17-year down cycle.
- During the latest cycle, new golf hole additions peaked in 1998, exactly 30 years after the previous peak.
- The latest up cycle took place over a 13-year period, with the total cycle encompassing 30 years.
- It has now been 15 years since new golf course hole additions peaked, and it looks like more decline is certain in the next few years.
- Although there was a loss of private clubs in the early 1990's, there was never an actual overall decline in the number of golf courses. For the first time in the modern era, the actual number of golf holes has declined every year from 2006 to 2012.
- There were some distortions in the growth of golf during this boom period, as the development of private golf holes directly correlates to trends with overall development of golf holes through the late 1980's.
- There was however a significant loss of private golf holes in the early 1990's, which can be attributed to the advent of high-end daily fee courses. With a membership no longer a prerequisite to quality golf, golfers could enjoy the variety of experiences available at brand new, high quality, pay-to-play layouts.
- In the current downturn, the development of private golf holes continued after 2005, despite the significant loss of public holes. This can be explained by the fact that while the golf course markets were indeed suffering, the residential real estate markets were still strong, or maybe ignoring the signs of trouble, but continued selling the lifestyle until roughly 2009.

- Since the great recession started, there has been a reduction in private clubs, as many have been converted to semi-private or public golf courses.
- The total number of golf courses in the United States has declined in every year since 2005. Just under 500 golf courses have been removed from the market during that time period, with 280 removed during the past two years.

FIGURE 1: ANNUAL NET CHANGE IN GOLF HOLES 1961-2012



Source: HVS Golf Services & The National Golf Foundation

Golf Supply, Market Conditions and the Current Development Cycle

The explosive growth of golf courses in the 1990's and early 2000's was due to a variety of different factors. While the edict of the National Golf Foundation to build a golf course a day to keep up with demand is often touted as the sole cause of the growth, it is our belief that the boom in development can be attributed to a variety of factors.

- Another prevailing theory is that the development of real estate related to golf courses was a significant cause for the overbuilding of golf courses, but in hindsight, these developments were only a part of the cause.
- While stand-alone golf development did occur during the upturn, a significant portion of development of golf courses centered on selling social status, lifestyle and green space that appealed to a large number of buyers.
- This golf course development took form in both residential development as well as resort development.
- Golf as a means for economic development, also contributed to the overbuilding in the market.

- Together, resort and real estate development-related golf courses represented about 50% of the change in the makeup of 18-hole golf courses developed since 1990.
- However, the most overlooked factor in the unprecedented growth in the game and the consequent overbuilding was that the availability of capital to build and acquire golf courses on a national level, became available to the industry for the first time.
- This new source of capital in combination with the social power of golf to define status, to stroke the ego, and the complementary perception of the golf course as a place where recreation, entertainment and business all coincided, the refinement of the golf course community, and the edict of the national golf foundation, combined to create a powerful incentive for golf and club development.
- This latest up cycle for golf development lasted for about 15 years, until the global financial crisis stopped the development of golf courses, and the major national lenders stopped loaning on golf assets altogether. The loss of national lenders resulted in a capital vacuum for many courses, and severely impacted the health of the industry.
- The lack of lenders in combination with 3 to 5 year terms for the golf loans created an inevitable financial crisis for the industry, as golf loans came due, and limited sources of refinance were available.
- We are now reaching the bottom of the market, as the health of the industry overall has stabilized. However, there is likely to be a continued decline in the number of golf courses for at least the next 2 to 3 years, and likely longer. The duration of this decline will in part depend on the return of debt financing to the market.

Golf Supply and Demand Characteristics

An examination of the number of golfers per course over this time period provides additional insights into the current state of the industry,

- Essentially we have the same number of golfers per course today as in 1988.
- Golfers per course peaked in 1991, but remained strong through 1997.
- Golfers per course started to decline in 1998, fluctuated in the early 2000's.
- Golfers per course have decreased every year since 2007.

The implications for the golf course industry are relatively simple. In order for the overall golf facility financial picture to improve, either golf courses need to be removed from the market, or converted to alternative uses, or there needs to be growth in the number of golfers and the frequency with which they play. By far the easier change is to eliminate supply, and this has

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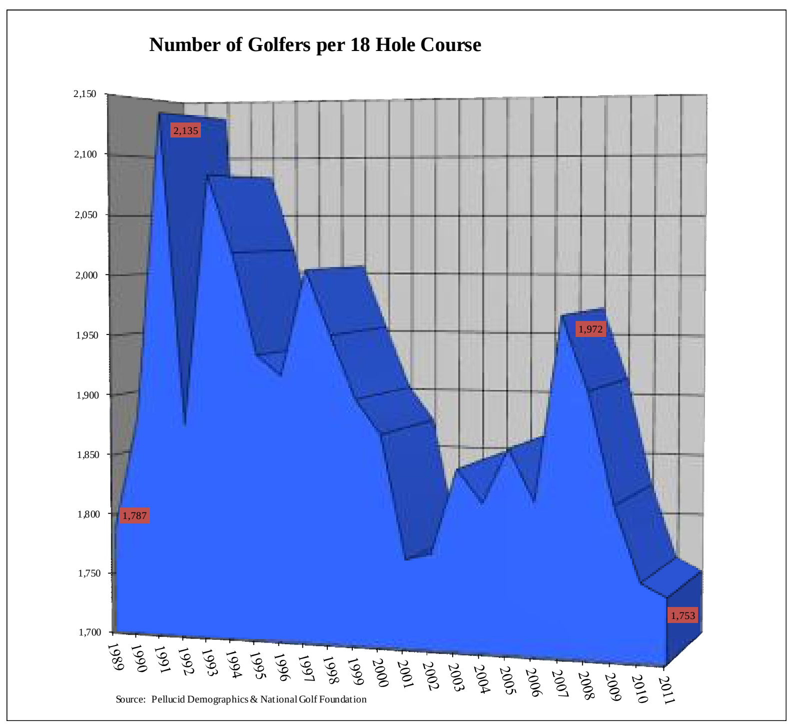


Source: HVS Golf Services & The National Golf Foundation been occurring over the past seven years and is likely to continue for the next three years. What is unclear is if there will be enough decrease in the supply to reach a stable equilibrium.

Loss of Supply and Longer Term Impacts

The extent of the loss of golf courses will help to determine the financial health of the remaining courses moving forward, but there are also “unintended” or other negative consequences arising from the reduction in supply.

The largest concern is that the older, less expensive, and easier courses are the ones that are being removed from the market. These facilities are typically targets as they were built some time ago, and are not of the same standard as the new courses. They are now infill sites, and the land value is high, and a golf course may not be the highest and best use of the land, and they were typically built in a “core” layout, so they are readily developable.

The loss of these entry level courses dictates that there are rising barriers to entry for new golfers, and more difficult to get golfers into the game. It follows that advances on the demand side of the game will be more difficult to achieve as these entry courses are removed and access to affordable and less difficult golf is lessened.

There are, however, a number of initiatives that have been developed over the past several years to grow the game. While they have achieved some success, they have yet to right the ship, as the number of golfers is still in decline.

What has become clear is that the core golfers are still solidly behind the game, and they will remain so in the near future. The fringe golfers have been much more difficult to keep involved and the new golfer harder to bring back. Solidifying the demand side is critical to the future of the game.

The Paradigm Shift

While the core golfers are rock steady, the occasional golfers drift in and out of the game. So why is it that occasional golfers churn every year? The usual culprits are the cost of the game, the time it takes to play, and access to playing partners. We believe that the heart of the matter is that events of the last decade have substantially changed people’s priorities and lifestyle desires. The events of September 11 were the first fulcrum for this change, and figuring out how to involve spouses, children and families in the experience became important. The global financial crisis put further constraints on the occasional golfers.

So in order to grow the game the challenges of hurdles of entry needed to be rethought, and the focus of these efforts needed to look to a different type of clientele.

While generating new golfers from the traditional demographic targets has had trouble succeeding, the ability to grow golfers in non-traditional ways was not something the industry had even tried.

The result has been a need for a paradigm shift in the perspective of the traditional clientele for the golf industry. These newly confronted challenges provide difficulties to the traditional models, but also opportunity to bring more people into the game and a chance to redefine the game for future generations.

These changes in perspective are taking place on two levels, with the first level occurring at the golf courses, with programs like Tee it Forward, and Golf 2020 as well as the advent of systems to learn the games such as

SNAG Golf. These programs and systems are implementing change to the perspective and nature of golf's clientele.

The second level is the changing face of many private country clubs to become more inclusive of the family and to diversify the amenities and services, so that they can sell a lifestyle that can cater to a broader audience. Additional changes to the structure of private clubs have occurred with a movement towards intergenerational memberships, and the linking of the generations.

These changes in perspective will undoubtedly have an impact on the growth and perception of the game and are integral to the health of the industry in the longer term. There are however additional changes in the way the industry thinks that need to occur in order to alter the financial prospects of the golf courses themselves.

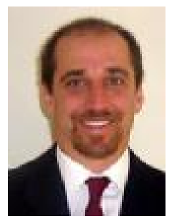
In the second part of this series, HVS will look at the financial implications to the individual golf course from the supply and demand characteristics of the market, the corresponding impact to golf course valuations, and the outlook for future golf course development.

About HVS

HVS is the world's leading consulting and services organization focused on the hotel, golf, shared ownership, gaming, and leisure industries. Established in 1980, the company performs more than 2,000 assignments per year for virtually every major industry participant. HVS principals are regarded as the leading professionals in their respective regions of the globe. Through a worldwide network of 30 offices staffed by 400 seasoned industry professionals, HVS provides an unparalleled range of complementary services for the hospitality industry. For further information regarding our expertise and specifics about our services, please visit www.hvs.com.

HVS GOLF SERVICES HVS Golf, Residential and Resort Community Consulting and Valuation Services, established in 2004 with headquarters in Boulder, CO, specializes in the market and financial analysis of golf, club, residential and resort communities. This division of HVS is charged with consulting and valuation services that evaluate the macro economic and financial environment surrounding the golf, real estate and resort development. Services include appraisal, valuation, feasibility, litigation support. For specific information on the division, please visit www.hvsgolf.com.

About the Authors



Darius Hatami is Managing Director of HVS Golf Services, based in Boulder, Colorado. Darius is a graduate of the University of Colorado and has been involved in various aspects of golf and community development for over 20 years. In 1995, Darius became part of the HVS family, and provided studies to hundreds of golf and resort community clients throughout the United States, Canada, Mexico, the Caribbean, Central America, Asia and Europe. His expertise encompasses valuation and feasibility studies as well as strategic, financial, residential economic planning, membership planning as well as integrating golf with residential and resort aspects of master planned communities.