

**Projecting the Supply of and Demand for Equity Memberships
and
Developing Processing Guidelines To Establish a More Balanced Relationship
Between the Two**

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4/27/2004

The Problem

Historically the Club has not timed its processing of Associate or Regular membership candidates with an eye to the availability of equity memberships either for Regulars when approved or for Associates when they turn forty. People have applied and were processed. Memberships were either available or not when the Regulars were accepted or the Associates turned forty.

The supply of approved Regular candidates has increased with time as a result of an increase in the number of Associate members. Associates are approved as Regular members and because of their age are able to delay purchase until their fortieth birthday. Although Associates can purchase an equity membership at any time without further processing, most tend to wait until they're forty to purchase a Regular membership.

However, the number of equity memberships available and sold in any given year has remained fairly constant over time. Unlike the growth in the supply of approved Regular and Associate candidates, only seventeen equity memberships have been offered and sold, on average, each year. (Note: this number does not include family transfers since the membership transferred is never in the market place for resale to approved candidates.)

The price of equity has risen sharply in the past few years. This increase might be related to demand, or the prospect of Associate demand, outstripping the supply of equity in the marketplace. It might have to do with the rising value of real estate in west Los Angeles, the Beach Club simply appreciating in value along with other real estate holdings. It might have to do with improvements in the Club, its goods, services, facilities and programs---the "intrinsic." It might have to do with the fact that the supply of beach clubs is fixed and the demand for "family escape opportunities" has increased. And it might have to do with the rising affluence of the westside community with the club a "retreat" they not only want but can afford. It probably has something to do with a combination of all of the above. The macro issues are out of the Club's control, but the micro demand issues---how many are approved to purchase and when---are not.

Herein lie two fundamental questions. Should the Board's efforts be to ensure that there's a membership available to purchase when needed---without consideration for its price---or to ensure that that memberships are "fairly priced" regardless of availability?

My observations would suggest that the Board wants to do both. They want to ensure that memberships are available for purchase and they'd like those memberships to be "fairly priced."

Therefore, if the Board wants to moderate future price increases, to assure approved candidates for Regular membership that an equity membership will be available for purchase within a year after their approval (i.e.---all approved Regular members are given one year from the date of approval to purchase an equity membership) and to guarantee Associates that equity will be available for purchase when they turn forty, a calculation needs to be made as to the number of applications that can be accepted for processing at any given time such that an equilibrium can be established between future supply and demand.

The following will attempt to outline such a calculation.

Issues

People who are selling equity memberships want to receive fair market value for their sale. They tend not to be "altruistic" when establishing a sales price. They base their pricing decision on micro issues (recent sales, the number of people who have been approved for the purchase of an equity membership---including Associates---the wait list, etc.) and on macro issues (the economy, west side affluence, the number of warm sunny days in the last six months). The micro information is given to them each month in a "Market Report."

The Club can't control the macro issues affecting a given member's pricing decision but it can impact the micro issues.

The Club has decided not to increase the supply side of the equation. Senior memberships are "out" and there is no interest in expanding the size of the membership base with a non-equity Associate type program. The club is "locked into" a natural supply stream of about seventeen equity memberships per year.

As for the demand side of the equation, the Club could control the flow of information to the sellers. If the Club chose not to supply the sellers with market information---the number of Associates who are able to buy, the number of people in "the pipeline," the number of people recently approved for Regular Membership, the recent selling price of memberships, the range of asking prices in the selling market---it could moderate the rise in equity prices. Ignorance would complicate a seller's pricing decision, and the prices would probably be lower than they currently are. To do so, however, would violate the concept of transparency that underpins the equity marketplace. It would, in my judgement, be unethical and therefore unacceptable.

Secondly, and more importantly, the Club could control the demand side of the equation by restricting the number of applications being processed at any given time. Controlling the number of buyers would help ensure that memberships would be available for

purchase when approved (for Regulars) or when turning forty (for Associates) and that those memberships would probably be “fairly priced” since supply and demand would be in closer balance.

There are several facts critical to any calculation of future supply and demand. A lot of guess work is needed to supply these “facts.”

1. What is the right number of available memberships versus candidates approved for purchase? One to one? Seventeen memberships on the market and twenty candidates approved for purchase? This might be a moving target and can be manipulated monthly based on actual experience.
2. The average length of time involved in processing an Associate or Regular membership candidate *from the time that the application is first seen by the Membership Committee* needs to be established. This will determine when processing should begin and approximately when the candidate will be in a position to buy a membership.
3. Candidates approved for Regular membership have up to one full year after approval to purchase an equity membership. They can choose to be “wait listed” until such time as a “properly priced” membership comes into the marketplace.
4. Family transfers can be processed at any time since their “purchase” is unrelated to the market. It should be noted that some who join as Associates eventually become “Family Transfers.” If this possibility exists it should be so noted at the time an Associate applies. Failure to do so will skew the number of “buyers” higher than it would otherwise be. On average, there are three such transfers handled on a yearly basis.
5. As the population ages, an actuarial assumption needs to be made as to when members of our growing number of “seniors” will go “non-resident.” Although the average number of members selling in any given year is seventeen, it may be that some years will have a significant “spike” because of deaths in our (ever larger!) elderly community. Guesstimating when that is could effect the processing calculation.
6. Calculating how many members will sell in any given year is as much art form (W.A.G.) as it is science. Members leave town unexpectedly, they divorce and liquidate, they die before their time, etc. The average is accurate in the aggregate but might be wildly inaccurate in the specific. When the variances will occur is anyone’s guess.
7. What percentage of people applying for Regular or Associate membership won’t “make it” through the membership process?
8. The “year of conversion” will be a consideration when choosing which Associate applications to process. Those whose “year of conversion” lands in a year with “room” can be processed while those whose “year of conversion” lands in a “fully booked” year will not.
9. Associates whose “year of conversion” has little room should be asked to forgo the Associate program and apply for Regular membership if there’s room for them at the time of process completion.

10. What percentage of Associate who become forty will choose to resign?
11. What percentage of Associates will simply resign during the course of their eight year “window” as an Associate?
12. What percentage of Associates will put their membership into “suspense” for a year at age forty?
13. Juniors aren’t part of the calculation since too many variables exist in their relationship to the Club, timing of purchase etc. Consider their application for Regular / Associate membership sufficient time to make them part of the larger calculation.
14. What percentage of Associates will purchase early, that is, before their fortieth birthday?
15. Given the number of variables involved, projecting outward for more than eight years (the maximum number of years someone might be an Associate) seems unnecessary.
16. The projections will need to be updated with current (not statistical) information on a monthly basis. The number of candidates being processed will be dictated by those updated numbers.

Many of these issues are impossible to determine, though one can make an educated guess given historical experience.

The following is a crude model that might be used to assist in calculating how many applicants can be processed at any given time. It’s not a “predictive formula” but a model that will help in controlling the flow of applications to the Membership Committee. There are lots of variables!

Year	05	06	07	08	09	10	11	12
(A)---Target Relationship between number of sellers and number of buyers (Example—20 buyers to 17 sellers / 15 buyers to 17 sellers)								
1. Projected number of equity memberships for sale.								
2. Number of Associates turning 40 in the year noted. (note---Associates have one year of “suspense” if they choose)								
3. Number of regular members being processed (does not include family transfers!) who will be approved and required to purchase. (Approved regulars can be “wait listed for a year)								

4. Total number of approved “wait listed” candidates and Associates who will be <u>required</u> to purchase in the noted year. (wait listed are those whose year “expires”)								
5. (Less): Guesstimate---number of those approved for Regular membership or waiting as Associates who will choose not purchase.								
6. Total number of candidates who will <u>probably</u> purchase in the year.								
7. Net number of Regular membership candidates that can be processed given “spots” available in the year (spots being Target Relationship---A--- plus or minus total number of those having to buy) (A.) – (6) = spots available								
8. Number of Associate applications to begin processing. (Date of their fortieth birthday to be noted in appropriate year, line two. Processing may be selective and not “in sequence” given the “year of conversion.”)								

Conclusion

To control the relationship between supply and demand, the Board needs to make a calculation---or guesstimate---on how many Regular and Associate membership applications should be “in the pipeline” for processing at any given time.

Once a preferred supply / demand ratio is established, the Board needs to calculate how many memberships should be in process, yielding a total number of buyers during any future year.

In determining how many should be processed and when, the Board needs to understand that some being processed will drop out of the process, some approved Associates will not buy, some Associates will buy early and even some approved candidates will choose not to buy once approved. The supply of memberships will vary above and below the norm due to untimely deaths, divorces, relocations and other strange and unusual occurrences.

In short, the Board will be using its good judgement to determine how many applicants to process at any given time after using whatever projections they choose to accept. Getting

it right will have to do as much with “art” as it does with any particular “calculation.” The Board’s guesstimate will require looking more deeply into the process and by so doing they’ll become more adept at anticipating how many applications to begin processing to yield the hoped for result eight years in the future.

Keep in mind that some sellers will object to “manipulating the market.” Any effort to impact demand will impact prices. Members wanting to maximize the return on their club investment might object to such “manipulations” since these efforts will probably slow the upward spiral in the price of memberships. Should their concerns be a consideration in the balance between supply and demand? Should the Board be concerned about the outgoing member or the incoming member? Isn’t the market being “massaged” already? Be prepared to respond if objections are voiced.

To make this system work, the Board will need to review its supply-demand projections each month and recalculate how many candidates should be “in process” at any given time. Doing so will bring the supply closer to demand, thereby slowing the rise in prices and, in theory at least, ensuring that memberships will be available for purchase when the approved candidate is required to buy.

Given the variables involved, this calculation will be “crude” under the best of circumstances. But “crude” will be helpful in arriving at a closer supply / demand relationship.