MODULE 7

Financial management for events: Part 2

University of Cape Town
Events Management short course

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Learning Outcomes:

LO3: Explain cash-flow management and its importance for an event.

LO4: Interpret the key financial statements produced for an event and for running an events company.

LO5: Explain return on investment (ROI) for events.

LO6: Explain some key financial processes.

LO7: Describe the financial challenges for an event and events company.

Disclaimer:

These notes are adapted from the University of Cape Town and GetSmarter's course notes for Module 3 of the Events Management elective offered as part of the blended version of the UCT Postgraduate Diploma in Management and Marketing.

1. Introduction

This set of notes sets out to explain how to manage cash flows for an event and how to calculate the return on investment (ROI) for an event. Additionally, aspects relating to how to accurately price an event and charge clients, as well as some guidelines as to how to manage an event successfully from a financial perspective will also be discussed.

2. Cash flow management

In a financial context, cash flow refers to the timing of income and expenditures in order to ensure that there is sufficient cash within an organisation at any given time to cover expenses within a given period (Shone & Parry, 2013:139).

Cash flow planning tips

Cash flow planning anticipates the flow of cash into and out of an event's budget. Paying invoices on time and tracking when income will be received is good cash flow. Good cash flow enables you to fund marketing and supplier deposits with your event timetable. Properly managing cash flow is vital to the success of any event and helps you prevent possible cash shortages.

Create a cash flow statement at the same time you create your budget. Aim to identify the in- and outflow of money from your budget. By developing your cash flow forecast, budget and event timetable, you are closer to understanding the amount of liquid funds needed to launch your event. This initial amount of money is required to fund activities such as website development, pay venue, and supplier deposits.

This phase can be problematic, as many companies and clients are looking to minimise their initial cash outlay and reduce financial risk. Often a compromise needs to be reached between the event management company and the client and part payments made according to an agreed upon payment plan.

The key problems caused by the lack of a proper cash flow plan are:

- Not being able to pay your suppliers. This tarnishes your relationships with suppliers for current and future events.
- Revenue shortage. You need to track money coming in and manage it appropriately.
- Exceeding your expenditure. Overspending is a big problem in event management. Stick to the allocated budget.

(Adapted from Bedouk 2014)

2.1 Deposits

The event manager has to carefully manage cash flow and ensure that there is enough money available upfront to cover all the initial costs that may be incurred (for example the deposits for venue hire and booking entertainment). The event manager will also have to decide whether the money will be obtained by raising funds, using profit from a previous event, or by asking attendees to pay a booking deposit (Shone & Parry, 2013:140).

The best way to manage cash flow for an individual event is to establish what payments need to be made and when. From there, the relative deposit amount needs to be secured from the client. The deposit amount should cover the deposits or payments to suppliers that need to be made prior to the event. The balance of the money should be paid preferably before the event or on the day of the event and then used to pay the balance of what is owed to the various suppliers. It is very important, especially for a small event business or a sole proprietor to receive the full payment before the event, if possible, as there are cases where clients refuse to pay the balance owed and it can be very costly to try to follow up and get the money back. Cash flow is also negatively affected and the event manager's relationships with their suppliers are soured.

The process outlined above reflects an ideal scenario, however, in reality it does not always work this way. Corporate clients, for example, generally will not pay more than a 50% deposit on confirmation and they may only pay the balance 30 days after the event. If arrangements have not been agreed upon with suppliers to allow for this, the events company will have cash flow problems (in that it will have to pay out more money than it is receiving). Event companies will often take out bridging finance to see them through the shortfall period, but this is of course costly, as the interest on bridging loans can be high. Larger event companies are able to manage their cash flow more creatively; they do not necessarily pay the suppliers of an event with that event's income; they may use another upcoming event's deposit to help pay suppliers instead. This can become an intricate process and is best managed by an experienced accountant.

Note:

Cash flow on an event will change at different times. For example, during the planning and conceptualisation phase, there will be no income as such, but there may be some spending. During the build-up phase of an event, there would be income and costs, (so money coming in and money going out). However, a larger amount of money may be going out than coming in during this stage. The money coming in should be from deposits paid by the client(s), and the outflow would be the deposits being paid to the suppliers and costs to build the event. The closedown of the event should see more money coming in than money going out, as most suppliers should already be paid and this is the time when the profit is generally realised (if there is profit generated).

2.2 Principles for managing cashflow

The following guidelines will assist you when putting cash flow management strategies in place:

- **Negotiate payment terms:** Always ensure that payment terms are fully negotiated upfront. Suppliers need to know when they can expect payment, and clients have to have a clear understanding of when their deposits and full payment for the event are due.

- **Research suppliers:** Conduct as much research about prospective suppliers and the nature of their business before entering into agreements. Find out what their payment terms are (can 30- or 60-day accounts be opened with them?), and whether they require deposits. It is useful to try and negotiate a contract that stipulates a small deposit upfront, with the balance being due after the event. Also, make sure that any potential extra charges, delivery, and set-up costs are discussed and agreed upon in advance.

- **Use purchase orders:** Ensure that each item that is ordered is stipulated on an official order form. This provides a form of control over expenses and ensures that there is proof of what the supplier is expected to supply.

- **Insist on descriptions:** Make sure that a full description of each item ordered is obtained.

(Allen et al., 2002:255)

3. Return on investment (ROI)

Return on investment (ROI) is a financial performance measure that is used to determine how efficient a given investment is, based on the percentage return relative to the initial investment it generates (Investopedia, LLC., 2016). It reflects how profitable an investment is for the investor, and whether it is a good use of the investor's money to contribute to that particular investment.

The formula for calculating ROI is as follows:

$$\text{ROI} = \frac{(\text{Gain from investment} - \text{Cost of investment})}{\text{Cost of investment}}$$

Video 1 illustrates how ROI works and how to calculate it in a few simple steps.

Video 1: How to calculate ROI. (Source: https://www.youtube.com/watch?v=eoAR8ZyAyoc)

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In an event management context, the sponsors, clients, and other stakeholders that provide funding for an event will use ROI to determine whether or not they are willing to invest in that same event again (or, if historical ROI data or feasibility studies are used, whether they want to invest in that event for the first time). On large events, ROI or feasibility studies are conducted during the early stages of event conceptualisation in order to determine whether the event is feasible or not. However, the dynamic nature of the event industry and its sensitivity to external factors does mean that investing in an event can be either extremely lucrative, or result in large losses depending on market conditions.

4. Pricing and profit

When deciding on a feasible ticket price for an event, the event manager has to consider multiple factors, such as the following:

- Will the ticket prices cover all the fixed and variable costs, marketing costs, depreciation, and future capital investment, and result in a profit (or at the very least, break even)?
- Is the proposed ticket price acceptable (affordable) to the target market?
- Are there different pricing packages that can be offered for different types of customers (such as senior citizen ad student prices, group discounts, or luxury and VIP packages)?
- Does the ticket price match the customer's perception of what constitutes good value for the event?

(Richards, 1992 cited in Oudtshoorn, 2010:174)

It is important to remember that ticket pricing should always be done in line with a careful consideration of the costs, and only once the costs have been identified can a realistic ticket price be established (Shone & Parry, 2013:142). Event managers should also conduct research to find out about their target market and what they would be willing to pay, and obtain quotations for all expected expenditures. The event manager must also factor in that the event may not enjoy full attendance (sold out shows or festivals are not a given), and as such it is wise to consider whether it is possible to break even when the event is only half full for example (Shone & Parry, 2013:144).

It is not financially feasible to host an event if all the costs are not covered, and if the goal is to make a profit, then tickets should be priced accordingly, as ticket sales often account for the bulk of an event's revenue.

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Keeping track of tickets:

The event manager must ensure that a designated team member is accountable for keeping track of the number of tickets sold, including any complimentary tickets that have been redeemed. At some events, tickets are designed in such a way that the ticket stub or counterfoil reflects the same number sequence as the actual ticket, allowing for easy record keeping (Oudtshoorn, 2010:178). By monitoring ticket movements, the event manager can maintain financial control over the event, and also avoid problems such as overselling or overcrowding.

4.1 Pricing strategies

The pricing strategy that the event manager selects will be based on the event's objective; an event that aims to generate a large profit, for instance, will follow a much more aggressive and competitive pricing strategy than an event that just wants to break even. There are three main pricing strategies that work well for events: cost plus pricing, premium (prestige) pricing, and discriminatory (differential) pricing.

How do I charge my client?

Charging your clients can be tricky. To help you be fair in your rates, you need to:

- Track your time.
- Know your hourly rate.
- Set your pricing and be confident about it.
- Know your process and share it with your clients.
- Explain the budget to the client in person if possible.
- Follow up promptly.
- Decide on your service charges.

4.1.1 Cost plus pricing

The cost plus pricing method is one of the most common pricing strategies. It is based on adding a mark-up percentage to the cost of a product or service in order to create a profit margin (Accounting Tools, 2016a). In its most basic form, the direct material, direct labour, and overhead costs for the product are added together, and then a predetermined mark-up percentage is added to this (hence the name "cost plus"). It is easy to think of this method as a way to determine how much profit you would like to make per ticket once you have covered all your costs.

For example, if you know an event is going to cost R1.1 million and you want to make a 20% profit, you add 20% (R220,000) to the costs and then work out how many tickets you would need to sell to generate R1,320,000. For example, at a ticket price of R200, you would need to sell 6,600 tickets (R1,320,000 ÷ R200) to reach a profit margin of 20%.

For large events like the FIFA World Cup, the fixed costs are very high and ticket sales, broadcasting rights, merchandise, and commercial sponsorships all need to be in place in order to realise a profit.

It is also worth noting that this method does have some disadvantages in that it does not take market-related factors such as the level of consumer demand, competitor pricing, and customer expectations of fair price into account. These factors will also have to be considered before making a final pricing decision.

4.1.2 Premium (prestige) pricing

Premium pricing (or prestige pricing, as it is sometimes referred to) is based on the premise that customers will purchase goods that are priced higher than competing goods due to their perception of the good having a superior quality or reputation based on the higher price (Accounting Tools, 2016b).

Some events have more appeal than others, and certain events are synonymous with certain expectations. These events create the perception of exclusivity and their price tags can therefore be higher, as there is a high demand. Prestige pricing methods help to further reinforce this exclusivity.

The greatest advantage of premium pricing is that, if the type of event lends itself to this pricing model, there is opportunity to attain very high profit margins (Accounting Tools, 2016b). The risk with this strategy, however, is that if the event manager misjudges the target market, exorbitant prices could result in many lost sales, and potentially lead to large losses on an event.

4.1.3 Discriminatory (differential) pricing

Discriminatory (or differential) pricing is a strategy that involves charging different prices to different target markets for the same product or service in order to maximise the amount of revenue that can be generated for that good (Boundless, 2015). For events in particular, this strategy is adopted to encourage greater attendance at an event and ensure that fixed costs are covered, because by extending ticket options to a diverse range of potential customers, more money can be made than by setting a standard price that excludes a whole range of potential customers that do not fall within that spending bracket (Shone & Parry, 2013:143). For example, at music concerts, golden circle and front row tickets are priced much higher than tickets at the back of the stadium, and at rugby matches the box tickets are sold at a premium price, while tickets far away from the field or behind the goal posts are cheaper.

Discriminatory pricing is based on yield management (or revenue management) practices, which aim to anticipate and influence consumer behaviour in order to maximise revenue from perishable resources (Oudtshoorn, 2013:175). Events are perishable resources because they are once-off occurrences, and selling event tickets after the event has passed cannot generate revenue. The same principle applies in the airline and hotel industries.

Yield management:

If you are interested in learning more about how yield management is applied in the service industry, Glenn Withiam's academic journal article entitled "A "4-C" strategy for yield management" explores the four strategic levers of yield management: calendar, clock, capacity, and cost, and explains how these factors are used in setting prices within the service industry in order to maximise revenues.

4.2 Other ways to generate profit at events

Selling tickets is not the only way to generate revenue at an event, and there are many other activities such as competitions or sponsorship that can contribute to revenue. Sponsorship will be discussed in more detail in Module 10, but for now, the list below provides some ideas for additional sources of income at events:

- Programmes and brochures
- Food sales (stalls or catering)
- Retail points, souvenirs, clothing, merchandising
- Photography and video services
- Transport and parking services
- Raffles, and competitions or games
- Broadcast rights (for major events)
- Arts and craft stalls (or other types of stalls)
- Cash bars

(Shone & Parry, 2013:155-156)

Digital monetization: The future of event revenue generation?

Following the technological and communication boom that the world has experienced over the last two decades, there is very little in the industry that has not leveraged the power of technology (and, more specifically, the internet) to generate revenues in some way. In this Event Manager Blog article, Aidan Augustin discusses the "untapped goldmine" that digital monetisation offers event managers, and explains how event managers can leverage digital communication and marketing opportunities to generate income for their events long before and after the actual event takes place.

5. Charging clients

Deciding how to price tickets for an event is one thing, but it is also important to consider how to charge a client. Event managers need to ensure that their services are competitively priced, and that they are not undercharging clients for the amount of work they are doing.

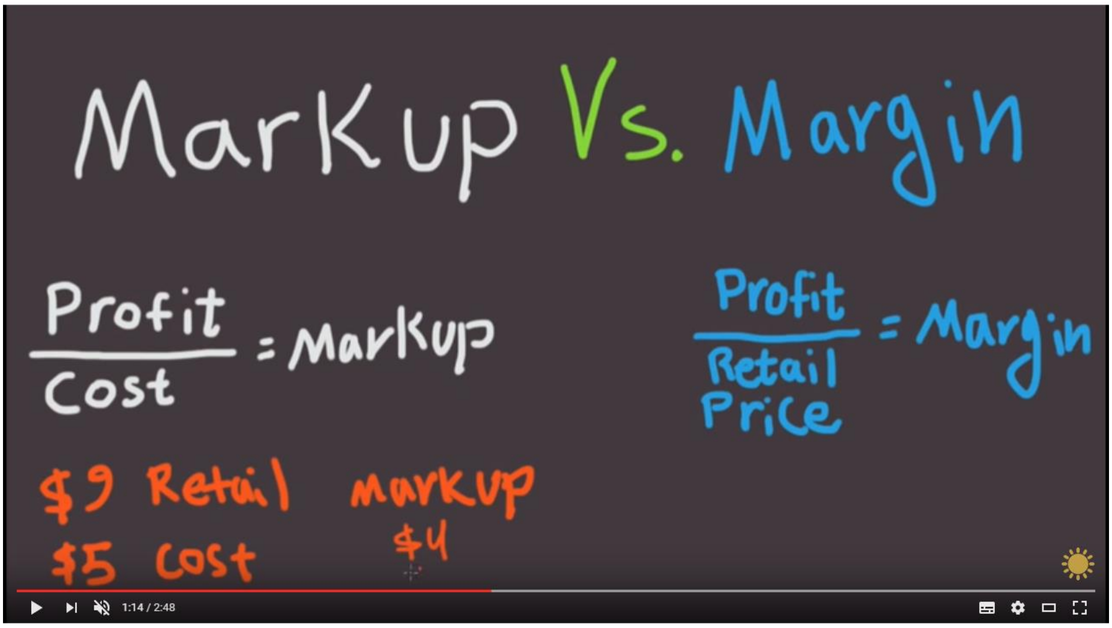
Event managers can base their fees on either:

- A flat project rate;
- A percentage of the cost of the job (a form of cost plus pricing);
- An hourly rate;
- A combination of percentage of cost and flat or hourly rates; or
- A commissionable rate.

More on fee structures

In this article, event planning expert, Rob Hard, explains each of the above-mentioned fee structures in more detail.

Video 2: Howard Givner from the Event Leadership Institute explains different pricing models and how to charge for event planning services. (Source: https://www.youtube.com/watch?v=Z1iivArIZSI)



Video 3: Difference between mark-up and margin. (Source: https://www.youtube.com/watch?v=ITdK3y7tA04&feature=youtu.be)

Mathematically, mark-up is always a larger number when compared to the gross margin. Therefore, many often think they are making more profit than they are. For example, if your mark-up is 20 per cent, it doesn't mean your profit margin is 20 per cent, the actual profit margin will be less.

Table 1: Mark-up percentages versus profit percentages and will be useful when putting together budgets.

Mark-up vs gross profit
15% Mark-up = 13.0% Gross Profit
20% Mark-up = 16.7% Gross Profit
25% Mark-up = 20.0% Gross Profit
30% Mark-up = 23.0% Gross Profit
33.3% Mark-up = 25.0% Gross Profit
40% Mark-up = 28.6% Gross Profit
43% Mark-up = 30.0% Gross Profit
50% Mark-up = 33.0% Gross Profit
75% Mark-up = 42.9% Gross Profit
100% Mark-up = 50.0% Gross Profit

Charging when an event is larger in size and longer in duration

Not all events are a day long and require short build and breakdown times. For mega events, hallmark events, or even conferences and exhibitions, for that matter, the event build-up may take a few days or even weeks as will its breakdown.

Consider the impact such extended preparation periods have on budgets. For instance, suppliers may need to charge the event management company more than one hire period (or the normal charge) because their equipment is at the event for longer than anticipated, rendering the suppliers incapable to rent out their equipment elsewhere.

Here is an excellent example of saving costs. For tables rented out to an event, say the normal daily rate is R45 a table and the client needs them for two weeks. The supplier agrees to two hire periods per week for the tables. This makes each table cost R180 in the budget. As a result, the client pays less and is likely to make more profit from their event.

6. Guidelines for financially successful events

Sometimes, regardless of the amount of planning and preparation done by the event manager, financial challenges can still plague an event. It is important to mitigate these potential problems, and Oudtshoorn (2013:179) provides some useful guidelines to ensure that the financial aspects of an event run as smoothly as possible:

- **Bills:** Ensure that all bills are paid on time (and not early). The only time that it is viable to pay bills before they are due is if a settlement discount is offered; otherwise, it is better to let the money earn interest.

- **Interest:** Try to deposit any excess money in an interest-bearing account, and conduct research to find financial institutions that offer high interest rates.

- **Extending credit:** It is not advisable to extend credit to clients; it is a good practice to send bigger clients pro-forma invoices before the event date in order to ensure that they make payment arrangements before the big day.

- **Cheques:** Limit the use of cheques (and credit cards), unless there is insufficient funds in the event company's bank account.

- **Relationship building:** Building a good relationship with the banker can stand an event manager in good stead in times of financial instability.

- **Recons:** If there isn't a designated accountant or financial manager, the event manager should ensure that they reconcile all their cheque accounts at least once a month in order to avoid an accumulation of these bank statements and a subsequent administrative backlog.

- **Deposits:** Deposit any money received on a daily basis in order to make provision for a better audit trail.

- **Communication to marketing:** Provide salespeople with clear instructions about what type of business (customers) is needed, at what times, and from which market segment.

Smart tip:

Challenges that may affect the event financially include the following:

- Not having a contingency budget
- Price undercutting in the industry
- Clients shopping around for the best price

- Poor attendance figures
- Poor perception of the event
- Clients with “champagne taste on a beer budget”
- Quoting blind without research and sourcing quotes
- Not double-checking quotes before they are sent to a client
- Not factoring in transport and labour costs associated with the event

7. Conclusion

An event manager, whether they own a business or work for an event company, can only benefit from knowledge regarding the financial workings of the company and should always have the necessary financial skills to run budgets and manage finances on events ranging from complex large-scale events to small private functions.

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