



“New and Better” Works

The rapid growth of Indian gaming has created an unusual dilemma for the leaders of many tribes. In the years following the passage of the Indian Gamin Regulatory Act, many tribes attempted to develop casinos. Unfortunately, it was unclear how successful these gaming properties would ultimately be, particularly for those tribes whose reservations were far removed from major population centers. Access to traditional capital markets was difficult. Amidst this uncertainty many casinos were developed using low-cost construction techniques or existing commercial structures were converted to gaming space.

As the industry matured and as properties were able to demonstrate their viability to the investment community, the cost of capital dropped and many tribes were able to replace their temporary structures with more attractive, full-service gaming/entertainment properties. Conversely, other tribes chose to keep their original properties and gradually expand them, all the while continuing to employ low-cost construction techniques. Many of these casinos generated outsized revenues relative to their invested capital. The logic for many in tribal leadership was, why incur additional debt by replacing low-cost structures when revenue streams were growing? The emerging dilemma was, why spend the money if one did not have to?

Fortunately, Indian gaming had its visionaries and they understood that by replacing their initial developments with new properties, they could better serve their existing markets, expand their reach into new markets and develop more diversified revenue streams. Further, their initial success allowed them to access capital at a lower cost. While debt was incurred, revenue streams far exceeded debt coverage and those casinos ultimately generated more income to fund tribal government services and improved the lives of their members. These operators understood that “New and Better” works.

Since revenues for most Indian casinos are not available in the public domain, it is difficult to quantify how building something new and better allows a casino operator to grow revenues. However, by examining the revenue performance of those publicly-owned casinos that operate in states that publish gaming revenue data, it is easy to see how building something new and better allows casino operators to grow revenue, expand their reach into new markets and achieve a sustainable competitive advantage. Two examples are presented.

The Blue Chip Example

The Northern Indiana gaming market is served by five casinos. The Horseshoe Casino and Resorts Casino (formerly Harrah's) are located just outside of Chicago. The Majestic Star and Majestic Star II (formerly Trump Indiana) are located in Gary, IN and the Blue Chip Casino is located 50 miles northeast of Chicago in the town of Michigan City, IN. In 2005 all of these casinos were located on riverboats, capable of cruising.

In January of 2006 the owners of the Blue Chip Casino replaced their riverboat with a single level barge. In addition, the boarding pavilion was rebuilt and new restaurants and entertainment amenities were added. Guests were now able to enjoy a more comfortable and spacious gaming environment with superior air handling and more gaming devices. Table 1 illustrates the performance of the casinos in the market before and after the opening of this new facility.

Table 1. Northern Indiana Gaming Revenue
Before and After Blue Chip Expansion (in Millions)

	12 Months	12 Months Prior	Post % Change
Blue Chip	\$236.1	\$291.9	24%
Harrah's/Resorts	\$285.4	\$324.7	14%
Horseshoe	\$420.0	\$433.6	3%
Trump/Majestic Star II	\$136.8	\$113.0	-17%
Majestic Star	\$149.3	\$134.4	-10%
Total	\$1,227.6	\$1,297.6	6%

Source: Indiana Gaming Commission
Blue Chip opened new barge on Jan 31, 2006
Harrah's was sold to Resorts in July 2005

Comparing the 12 month period after the opening of the expansion to the prior year period, Blue Chip increased gaming revenue by \$56 million or 24%. During that same period, the two casinos in Gary saw declines of 17% and 10% respectively. Not surprisingly, the casinos in Gary offered gaming environments that were far less attractive than Blue Chip's.

The L'Auberge Example

Lake Charles is just south of Interstate 10 in Western Louisiana. Until 2005 the market was served by two riverboat casinos: Isle of Capri and Harrah's. Both properties featured traditional riverboats that were built over a decade earlier when the State of Louisiana required casino

riverboats to cruise. Each property operated out of a boarding pavilion with a simple suite of amenities.

In May of 2005 Pinnacle Gaming opened L'Auberge du Lac, a \$300 million casino resort that featured a four-star hotel, a single-level casino barge, attractive public spaces, a wealth of dining options, a spa, golf course and a themed poolscape, complete with a lazy river. Table 2 illustrates the performance in this market for the three months prior to the opening of L'Auberge and the three months after its introduction.

Table 2. Lake Charles Gaming Revenue
Before and After L'Auberge du Lac Opening
(In Millions)

	3 Months Prior	3 Months Post	Post % Change
L'Auberge du Lac	N/A	\$48.0	N/A
Harrah's Lake Charles	\$39.9	\$37.4	- 6.3%
Isle Lake Charles	\$44.3	\$41.0	- 7.4%
Total	\$84.2	\$126.4	50.1%

Source: Louisiana Gaming Control Board

L'Auberge opened in May, 2005

In its first three months of operation, L'Auberge earned \$48 million, far more than its two established competitors. Harrah's saw a 6.3% drop in gaming revenue and Isle experienced a 7.4% decline. More significant was the fact that the overall market grew by over 50%. In other words, L'Auberge demonstrated that there was a considerable amount of latent demand from gamers who found the existing casinos unappealing. Until the opening of L'Auberge they had forgone gambling in Lake Charles rather than play in facilities that were not to their liking.

In September 2005 Hurricane Rita struck and caused significant damage to the region. Harrah's riverboat was dislodged from its moorings and destroyed. Both the Isle and L'Auberge sustained less damage and were able to re-open. However, rather than rebuild, Harrah's chose to exit the market. The company may have realized that the cost of building a new property that could effectively compete against L'Auberge was too great.

Today, L'Auberge dominates the Lake Charles market. In fact, it is in the midst of constructing a new hotel tower and is developing a second casino resort adjacent to its existing operation.

Both of these examples demonstrate that when a casino operator builds new gaming and entertainment facilities that are decidedly better than what was previously available, they are able to extract more gaming revenue from their markets by appealing to people who did not find the previous gaming products appealing and, as in the case of L'Auberge, they were able to gain a sustainable competitive advantage that its rivals were unable to overcome. The lesson here is that new and better gaming and entertainment facilities work, and they work well. ♣

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