



Build Your House Out of Bricks

"The most dangerous strategy for tribes with temporary casino structures or inadequate facilities is to maintain the status quo. By failing to reinvest in their casinos and to better meet the needs of their markets, these tribes put their most important assets at risk."

About fifteen years ago, Steve Wynn, then CEO of Mirage Resorts, gave a speech to an audience of alumni and students at a prestigious college of hotel administration. He began by reciting Grimm's fairy tale of The Three Little Pigs. At first the audience collectively laughed as Mr. Wynn began his recitation but it soon became evident that Mr. Wynn was to recite the entire fable. And so he did.

Mr. Wynn later explained that the lessons taught in this fairy tale were important to the hospitality industry and equally applicable to casino developers as to children. Build a house out of bricks rather than straw or wood and you will be able to weather any storm or wolves that threaten your house. Since its opening in 1989 the Mirage withstood the introduction of more than a half dozen new competitors. Fifteen years later the Mirage continues to compete with the best properties in Las Vegas. In the coming months the Mirage will introduce new nightclubs, restaurants, a Beatles themed Cirque du Soleil show and an improved volcano attraction. Room rates and slot win per unit have and continue to remain well above the market average. After all, the property was built out of bricks.

Mr. Wynn's construction strategy was revolutionary for Las Vegas. Prior to the introduction of the Mirage, casinos and casino expansions were not noted for quality design, efficiency and reinvention. In fact, many were built as cheaply as possible. Properties built with savings in mind suffer today from significant problems including inadequate elevator capacity, insufficient plumbing capacity and other deficiencies that impact guest satisfaction. Today, several strip and downtown properties are in such a poor state that wholesale replacement is their only recourse.

The lessons learned in Las Vegas are certainly applicable to Indian gaming operations. After the passage of the Indian Gaming Regulatory Act in 1988 many tribes struggled to secure financing for their emerging gaming operations. As such many were forced to build temporary structures or convert aging bingo facilities into casinos. With the introduction of slot machine gaming at these properties, gaming revenue soared. Tribal governments and their members were the main beneficiaries of the casinos' success.

Some tribes understood the importance of sound master planning and eventually replaced their temporary structures

with more attractive facilities that utilized more traditional construction techniques. These tribes understood the risk associated with the assumption of debt and the short-term reduction in income to service that debt. They also recognized the importance of building quality facilities that could evolve to meet the changing needs of the marketplace. The rewards from implementing such strategies were more attractive and efficient properties that provided better gaming entertainment experiences to customers and ultimately higher income streams. Most important, these properties can now withstand the onslaught of any new competitors entering the market.

Other tribes have and continue to operate casinos in structures that were never meant to be permanent facilities. Rather than invest in new facilities that could ultimately provide more income, tribal governments simply ask that their gaming operations increase the amount of money they upstream to fund government services without regard to market conditions, higher operating costs or the introduction of new competition. The expectation is that these temporary casino facilities will continue to grow revenue without capital reinvestment. After all, the customers have nowhere else to go. In defense of these tribal governments, essential services must be provided and periodic income distributions are important to alleviate poverty. However, without reinvestment tribal leadership puts its most important assets at risk.

Beware of the Wolf

Many tribes operate casinos in markets that have little or no competition. Without the threat of new competition, tribes may be disinclined to take on debt and experience a short-term diminution in income. However, this strategy is often short-sighted and can expose the tribe to significant risk.

The greatest risk is the introduction of new competition and the effect it has on weaker, less attractive properties. While many would assume competition only comes in the form of another tribe, or perhaps a state-sanctioned casino opening within a tribe's primary market, competition can appear in other forms. The most prevalent one today is the introduction of slot machine gambling at race tracks. Other

forms of new competition include the introduction of new video lottery terminals that are operated by state lottery commissions. Like electronic bingo machines these VLTs continue to evolve and can offer the same entertainment features as traditional slot machines. They could eventually appear in taverns, convenience stores, hotel lobbies and other non-traditional locations that could siphon off discretionary gaming dollars.

Another threat is the expansion and replacement of Indian casinos by other tribes in what may be adjacent markets. When competitors in neighboring counties replace their gaming operations with more attractive facilities, they alter customer expectations. Players that see and experience casinos with higher levels of quality may forego visits to their local casino for less frequent, but more enjoyable experiences at nicer properties that offer accommodations, multiple dining venues and non-gaming amenities.

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The opportunity to operate a casino is not afforded to everyone. It is in fact an exclusive right to do business. No one can dispute the benefits that gaming has brought to North American Indian tribes. However, casinos are assets that must be nurtured and protected. They must be allowed to evolve to better meet the needs of customers. Tribal leadership in turn must understand the wants and needs of their markets, design properties to serve them, assume a modest amount of risk in order to invest in the future and temporarily reduce demands for ever increasing income to fund tribal services.

The lessons of the Three Little Pigs are obvious. The wolves are out there and only the houses built out of bricks will survive. ♣

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