

Tue Nov 10 12:09:34 PST 2015

b13432758      Last Updated: 07-21-2014      Created: 07-12-1989      Revisions: 12

TITLE      Casino gaming in Atlantic City : a crisis ahead? / Janney Montgomery Scott, inc  
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INC.

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June 2, 1989  
INDUSTRY UPDATE

Marvin B. Roffman  
Vice President

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## CASINO GAMING IN ATLANTIC CITY

### A CRISIS AHEAD?

#### Atlantic City, New Jersey - Top Heavy in Debt - Houses of Cards

Five years ago Atlantic City had nine casinos which generated a casino win of \$1.77 billion and profits of \$168.7 million. Last year the city's twelve casinos won \$2.73 billion from its bettors and reported profits of only \$14.7 million. There were several nonrecurring writeoffs included in last year's numbers, but even looking back to 1987's profits of \$73.9 million the results are still poor. For example, 1987's bottom-line is equivalent to less than three cents profit for each dollar of revenues and about two cents return for each dollar of invested capital. More disturbing is the level of debt that has been piled on. Long-term debt on the city's casinos now totals over \$2 billion, and next year, when Donald Trump opens the Taj Mahal, total debt will exceed \$3 billion. What's more, interest expenses totaled a whopping \$293.5 million last year, equal to 9.5% of total revenues and twenty times profits. Next year's interest expenses will exceed \$400 million.

#### RECOMMENDATION: UNDERWEIGHT

Next year, Atlantic City casinos face a big jump in new gaming capacity and a few operators face huge increases in debt service. We believe there is no longer any margin for a slowdown or decline in revenues. We believe a slowing economy can put a few operators over the edge. Atlantic City has just lost its first casino, the Atlantis, and we believe there will be more failures. Nevertheless, through Atlantic City's near-term gloom we see some timely investment opportunities. Two of the most outstanding casino operators, **Caesars New Jersey (CJN-\$25)**, a pure play in Atlantic City, and its parent **Caesars World (CAW-\$36)**, are companies that have outstanding management and excellent growth prospects. CJN is reviewed on page 7 of this report. Caesars World owns 86.6% of Caesars New Jersey and has two other casinos including Caesars Palace in Las Vegas, one of the most profitable casinos in the world. The Palace is currently undergoing major renovation, which will increase its casino area by 47%. We estimate CAW's cash flow this year in excess of \$220 million. At the current market price of \$36, CAW is selling at a 20% discount to the market.

## Debt With a Capital "J"

Atlantic City casino's balance sheets are so leveraged that for every one dollar in equity there is six dollars in debt. Most of this casino debt is rated in the "junk" category which means that it is speculative whether the borrower has the capacity to pay interest or repay principal in accordance with the terms of the obligation. Last month, the Casino Control Commission would not renew the Atlantis' casino license, and the financially ailing casino closed its gaming floor on May 22. We expect to see more of this. Next year, even with the recent closing of the Atlantis, Atlantic City's gaming capacity will increase by an additional 20% with the opening of the Taj Mahal, the largest and most expensive casino in the world. We estimate the Atlantic City gaming market is currently expanding at an 8% annual rate. But we do not think that level of growth is sustainable in a recessionary environment. We are most concerned about the staying power of a few of the highly leveraged casinos next year when the Taj opens. Our biggest near-term worries are Resorts International and the Claridge, but the Taj itself looks like a big gamble.

## An Expensive Place To Operate

Compared to their cousins in Nevada, Atlantic City casinos' pay a hefty price to keep their doors open. The state's two regulatory authorities, the New Jersey Casino Control Commission and the Division of Gaming Enforcement, currently police and regulate the 11 locations with a staff of 1,080 and a budget of \$59 million. New Jersey's casinos foot the bill for regulatory expenses in assessments and licensing fees in addition to an 8% levy on casino revenues and a 9% corporate income tax. What's more, the casinos have an additional obligation to invest 1.25% of revenues in projects to improve the city. Exacerbating the problem is a recently proposed plan that would put a new luxury tax on room comps at a rate of 12%. Had this tax been in effect last year it would have cost the twelve casinos an additional \$12 million in taxes. Nevada's casino have a much friendlier environment, they pay a maximum tax of 6.25% on casino revenues, but there is no corporate income tax. Nevada's two regulatory agencies operate with 372 employees on a budget of \$15.7 million to police 285 gaming locations.

Nevada's casino profits have been in a strong uptrend over the past five years having risen from \$180.5 million in 1983 to a record \$689.2 million in fiscal 1988 (June 30). Unfortunately, a few of Atlantic City's casinos have yet to show a profit. Last year seven of the twelve casinos lost money. Also in the first quarter ended March 31, seven casinos reported a loss. Some of those operators point to the excellent numbers on the operating line, (before taxes, depreciation, amortization, and interest charges) eagerly awaiting the day when debt will be paid down and bottom line numbers explode on the upside. A few of those

operators remain wishful thinkers, piling on hugh debt, hoping that if everything goes according to plan, their investments will turn out to be bonanzas sometime down the road. Because the USA has been in its longest economic expansion since the Second World War, many of Atlantic City's young casino executives may not remember how devastating a recession can be to the industry. During the last recession, between the fourth quarter of 1980 and the first quarter of 1982, the then nine casinos racked up combined losses of \$97 million. We believe a loss of that magnitude could be devastating today for two reasons. First, balance sheets are leveraged to the hilt. And secondly, Atlantic City is now a much more competitive marketplace. We see some tough times ahead for Atlantic City's casino operators over the next couple of years, maybe even a crisis or two. We expect to see a speedup in the consolidation of the industry - more of the rich get richer, poor get poorer syndrome.

### Recap of Last Year

Last year about 38% of U.S. gaming action took place in Atlantic City. On May 26, Atlantic City celebrated its eleventh anniversary of casino gaming. During this period it has gone from zero to a \$2.7 billion gaming market. In the last five years the East's only gaming market has grown at a compounded annual rate of 9.0%. Over the next several years we think the market growth will slow to between 7% and 9%. Our projection reflects our outlook for a slow growth economy, as well as the fact that percentage increases from a base approaching \$3 billion are inherently smaller.

Over the past six years there have been many changes in the management and ownership of the twelve casinos. But perhaps the biggest change is in the makeup of the revenue stream itself. In 1982, table games generated almost 54% of a total \$1.5 billion win. Today, slot machines are where the action is, and last year slots generated 54.6% of the gaming win. This trend continues, and last month the city's 19,537 slot machines accounted for 58.3% of the combined win. Over the past six years Atlantic City's slot win has increased at a compounded annual rate of 13.6% compared to a 7.6% rate for table games. On the surface this would appear to be a big plus for the casinos. That's because slot machines are consistently the most profitable department in a casino. Unfortunately, the majority of Atlantic City's operators have not been able to translate the big increases in slot win to bottom line performance because, in our opinion, they are spending too much to counter the recent flat performance in table game play.

In an effort to build table play a number of the casinos have dramatically stepped-up promotional outlays. For example, complimentaries and credit issued to players have been rising sharply. Last year's complimentaries totaled \$721.9 million, up 19% from the previous year. Credit play (a form of interest free

loan to the bettor) has also been generous and expanded by an additional \$209 million last year, to a record \$2.2 billion.

Another trend hurting the bottom line is the is the step-up in giveaways to the slot players. All of the casinos are aggressively courting the so called "high-roller" slot player - that is the player who feeds dollars rather nickels or quarters into their machines. This high-end player typically is a drive-in customer as opposed to the majority of the slot players who are bussed in. Last year the casinos bussed 13.5 million passengers into their casinos, only 1.6% more than the previous year. Prior to last year, the growth in the expensive bussing programs was explosive. Now, the casinos are focusing more and more on the drive-in business, thanks to the big increase in parking accommodations. These desirable drive-in customers typically leave \$75-\$100 at their favorite casino. On the other hand, the typical bus patrons are primarily slot players leaving behind about \$35-\$40. To lure bettors the casinos spent \$265.5 million in coin giveaways last year, a whopping 21.6% increase over the previous year and 50% more than two years ago. An increasing portion of these giveaways is going to the drive-in customer and virtually all of this was in the form of rolls of quarters. The casinos hope the recipients will then deposit these quarters in their slot machines.

We estimate that last year Atlantic City's twelve casinos offered a bus package with an average value of \$22 per passenger. The push for the drive-in slot patron has also helped bring down the slot hold percentage (what the house keeps) from 12.2% in 1987 to 11.6% last year. While six tenths of one percentage point does not sound like a meaningful number, on a slot handle (what is deposited in the machines) of \$12.9 billion, the casinos gave back an additional \$77.2 million more last year than they would have paid under the hold percentage level of 1987.

Another explanation for the more generous slot payouts relates to the games themselves. The hold percentage on video poker was only 8.4% last year, a much "looser" game machine than conventional reel machines, which typically hold in a range of 11% to 15%. As a result, video poker play was up almost 38% last year as players recognized they could play these machines longer. Harrah's Marina Casino Hotel, owned by Holiday Corp. (HIA-\$48), has the loosest slots in town. Bally's Park Place and Resorts are programmed to hold 16%-17% more than Harrah's. Harrah's not only offers the slot players the best odds but they also rate very high marks on the bottom line. Harrah's operating margins, at 29.1%, are close to Park Place, which boasts the highest at 31.9%. Harrah's has the least aggressive bussing program, (373,000 players last year) focusing on the more affluent drive-in customer. The better slot payout also gives Harrah's players more time to lose their money. Their drive-in customers do not have to stop playing to catch a bus. On the other hand, Park Place, with no self-parking, has an aggressive bussing program (over 1.1 million players last year). It

has only six hours in which to take its bettor's money before the bell rings. Obviously, both casinos have developed a formula for success and a loyal and growing customer base, and that's the name of the game in the casino business. We would like to examine each of Atlantic City's casino and see how the action is.

### Let's Take A Walk On The Boardwalk

We start our walk on the famous 119 year old, wooden walkway at the west end of the four mile Boardwalk, traveling east toward the marina area. Our first casino on Boston Avenue is Bally's Grand.

**Bally's Grand** - This casino was born the Golden Nugget (GNG-\$23) in December, 1980. Under its previous management, the casino was one of the most successful in Atlantic City. Then in the spring of 1987, Bally Manufacturing (BLY-\$25) purchased it from GNG for \$440 million. Since the property changed hands the Grand has been loosing market share, and more important, it's operating profits tumbled from \$62 million to \$54.5 million last year. In 1988 its casino win dropped by 8%, and through the first four months of this year the Grand's win declined 4% compared to the same period a year ago. Management has been building a crosswalk connecting its garage to its casino over busy Pacific Avenue and is converting its garage to increase self parking. While the Grand has been a big disappointment for Bally, it should take comfort that its other Atlantic City casino, Park Place, is one of the most profitable in the world.

**Tropworld** - After a three block walk to Brighton Avenue we're at Ramada Inn's (RAM-\$12) flagship hotel. This casino opened as the Tropicana in November, 1981. It has not been a runaway success. By the end of 1982, Tropicana had racked up losses in excess of \$40 million. Then things started to get better and Ramada decided to pull all stops and finance a \$200 million expansion of the property, which was completed last September, on time and under budget. The new Tropworld is the city's largest property, boasting 1,000 rooms, 87,760 square feet of casino space, 147 table games, and 2,368 slot machines. More important this new property has been turning in some impressive numbers. In the first four months of this year Tropworld's gaming win jumped 25% over the year ago figures. Management has been spending aggressively and even buying some of its new business, to promote its themed amusement concept. For example, in the first quarter ended March 31, Tropworld's revenues increased \$15 million, but its operating costs jumped by \$17.7 million, so it reported a net loss of \$6.0 million compared to a loss of \$746,000 last year. Most important for Tropworld is the ability to sustain its recent revenue momentum and trim its overhead in order to cover the \$13.0 million increase in this year's interest expenses.

**Atlantis** - After a five block walk we are at the Atlantis Hotel.

The New Jersey Casino Control Commission ordered Atlantis' casino to close down on May 22nd. On April 15, Donald Trump agreed to purchase the Atlantis for \$63 million and turn it into a luxury non-casino hotel. We believe there will be more casino failures.

**Trump Plaza** - The Convention Hall separates the Atlantis from one of best run casinos in town, Trump Plaza. This property was born Harrah's at Trump Plaza in May, 1984. Mr. Trump bought out his partner Holiday Corporation, owner of Harrah's, in 1986 for \$76 million. After Mr. Trump completed a 2,700 space parking garage and extensively upgraded the property, business really took off. Because of its strategic location, about a one minute drive from the busy Atlantic City Expressway, the desirable drive-in customers have been flocking to the Plaza's casino. Last year this property enjoyed the biggest percentage increase in casino win - up 23% over the previous year to \$300 million. Through the first four months of this year the Plaza was number one in casino win, taking in \$100 million.

Directly adjacent to the Plaza is the Penthouse site that Mr. Trump recently purchased for \$56 million. The Penthouse property was supposed to have been developed into a casino hotel in the early 1980's by Penthouse magazine publisher Bob Guccione. Mr. Guccione actually started construction but ran out of cash. In 1987, Pratt Hotel Corp. (PHC-\$1), operator of the Sands Hotel Casino, agreed to pay \$61 million for Penthouse's property, but the deal never closed. In the meantime Mr. Guccione claimed that his contract with Pratt expired last December, and in March he put the site back on the market, agreeing to a deal with Mr. Trump. Pratt is suing both Mr. Trump and Mr. Guccione, and we think the outcome will be determined in the courtroom. The trial has been scheduled to begin July 24.

**Trump City By The Sea** - If Mr. Trump's purchase prevails, he then plans to build a 1,000 room, non-casino hotel on the site. If Mr. Trump also prevails in his bid for the Atlantis, he would control the most important real estate in Atlantic City. In effect, after the completion of his third Atlantic City casino, the Taj Mahal next spring, Mr. Trump would control 31% of the city's gaming area and 39% of its first class hotel rooms (including Penthouse and Atlantis). He would also own about 40% of hotel convention space, 35% of the parking spaces, and close to one half mile of Boardwalk frontage. And he would control most of the real estate around the proposed convention center. We believe the new convention center, which is scheduled to open in the early 1990's, will play an important role in Atlantic City's future success. If Atlantic City is to shift from its current "day-tripper" type of market, where the average visitor stays in town for about eight hours, to more of a year-round destination resort it must have more first class hotel rooms and the convention center. Mr. Trump will have most of those rooms and enough public space in his properties to handle his own conventions. Unfortunately, Mr. Trump's company is

private, so there is no way to participate in the profits.

### **Caesars Atlantic City - Our favorite Atlantic City Casino**

Caesars New Jersey (CJN-\$25), operates one of Atlantic City's premier casinos. It is located one block from the Trump Plaza. Last year Caesars edged out the top spot in casino win, reporting \$308 million. Its casino has been number one in this category for the last four consecutive calendar years. Most important, its operating margins were 24.4% compared to the industry average of 18.1%. Caesars has been a consistent leader in the high-end of the gaming market.

CJN is the only stock we are recommending for purchase as a pure Atlantic City play. Net income for the first nine months of fiscal 1989 (July) was \$26.3 million, or \$1.62 per share, compared with \$23.0 million, or \$1.42 per share, in the fiscal 1988 nine-month period. Revenues for the nine months of fiscal 1989 totaled \$251.1 million, compared with \$238.2 million a year ago. The improvements primarily reflect increased casino play, greater marketing efficiencies and reduced interest expenses. For fiscal 1989 we are looking for a 17.5% improvement in the company's earnings, to an estimated \$38.3 million or \$2.35 a share, a 17.5% improvement over the reported \$2.00 in fiscal 1988. Management is about to construct a \$33 million parking garage on its property which should help attract a host of new customers and prepare the casino for the nineties. Currently this casino pays 19.3% of its casino's pretax profits plus a rental fee of \$2.7 million annually to a privately-owned partnership which owns the land on which the casino sits. In fiscal 1987 Caesars paid its landlord \$9.4 million and fiscal 1988's payment was \$14.5 million. Caesars has exercised its option to purchase the property outright for \$38.7 million, and the purchase will be effective on June 1, 1989. We believe ownership of the property will greatly enhance the casino's long-term earnings prospects. For example, had Caesars exercised its option in June, 1987, we estimate last year's net income would have been about \$6 million higher than the reported \$32.5 million, and earnings per share would have been \$2.36 (\$0.36 a share higher than the reported \$2.00). This assumption was based on a 10% interest rate on the borrowed funds.

At \$25 a share CJN is selling at 10.6 times this year's estimated earnings and at a 20% discount to the S&P 400. We consider CJN undervalued and rate its shares a Buy for aggressive investors.

**Bally's Park Place** - Bally Manufacturing owns Park Place, one of the most profitable casinos in the world. Its operating profit margin of 31.9% is second to none. First, it has an outstanding location in the center of the Boardwalk and across the street from two feeder casinos - the Claridge and the Sands. Most important, it has firm control over its operating expenses. Its complimentary



policy is the lowest in town as a percentage of revenues. In terms of payroll and interest charges to revenues, Bally operates lean. Credit play is also low. In early May, Bally began to bring on stream its new 800 room hotel tower, and we believe they will also expand their casino by about one third. Bally's Park Place is a real money machine. Bally's management wishes its three other casinos (two in Nevada) were as profitable.

**Claridge** - Across the street from Park Place is the Claridge, one of Atlantic City's problem casinos. Since opening its doors in July, 1981 it has racked up losses of \$160.4 million. It has never had a profitable year. Del Webb originally owned the Claridge but sold it to a Limited Partnership in 1983. After the sale Webb undertook significant management and financial obligations to the purchasers. A group of private investors, (led by Alfred Luciani, a former president of the Golden Nugget in Las Vegas) is trying to close a deal to purchase the Claridge. The problem is raising the funds, which could approach \$100 million. If the Claridge is not sold by the end of this year, and if it cannot raise additional financing, it could face severe liquidity problems and a license holder (Del Web) with no economic incentive to provide additional working capital.

**Sands On the Park** - Pratt Hotel Corp. owns the Sands which is directly across the street from the Claridge. The Sands was born The Brighton Hotel Casino in August, 1980. Unfortunately, its former owner, Greate Bay Hotel and Casino, ran into serious operating problems and sold the property to Pratt in 1981. Pratt installed new management and turned the operation around. The property has been substantially upgraded and a 1,850 space parking garage has been added to its original 500 spaces. A people mover has been installed to facilitate walk-in traffic from the Boardwalk. Casino revenues were \$205.7 million last year, 54% more than its next door neighbor, the Claridge. More important, the casino has recently been paying more attention to the bottom line. In the first quarter ended March 31, the Sands' revenues rose 12.8% to \$54.7 million while operating profits improved 82% to \$11.9 million. We estimate the Sands' operating profits will increase 35% to \$52 million this year. While its Atlantic City property is doing well, Pratt Hotel Corp. also owns seven non-casino hotels as well as an interest in a casino hotel in Puerto Rico. Unfortunately, a few of the other properties are not doing well. Pratt's managers have announced that they intend to focus their future activities in the domestic gaming market, particularly Atlantic City. They are intent on pursuing the litigation concerning the Penthouse site in order to develop their second Atlantic City casino project. In the meantime they are trying to sell off the problem properties, but this could take time during which they are dragging down Pratt Hotel Corporation's earnings.

**Resorts International** - From the Sands to Resorts we must walk one-half block back to the Boardwalk and then six blocks east to

Atlantic City's first casino. When Resorts opened its doors in May, 1978, it greeted long lines of anxious gamblers. Resorts had the market to itself for 13 months, and its monopoly caused its operating margins to be 55%. From there on, it was all downhill. The company's major problems started when it decided to build its second Atlantic City casino, the Taj Mahal. Construction of this huge project began in 1982 and for the next five years ate up most of the company's cash flow. After years of mismanagement and over \$500 million in outlays, construction on the Taj ceased. After its founder, James Crosby, died in 1987, Donald Trump acquired voting control from the founder's estate by buying up most of the class B shares. He then made an effort to take the company private, but fortunately for him Merv Griffin made him an offer he could not refuse. Mr. Griffin purchased Mr. Trump's shares for \$135 a share (\$96 million) and another \$63 million to terminate Trump's lucrative management contract with Resorts. Trump, in turn, agreed to buy back the unfinished Taj Mahal for \$273 million. Mr. Griffin then took Resorts private by purchasing Resorts' class A shares for \$36 a share (\$205 million). To finance the deal, Mr. Griffin and Drexel Burnham convinced investors to buy \$325 million in junk bonds.

Resorts has been loosing market share at its casinos in Atlantic City and in the Bahamas. For example, last year Resorts' win grew 1.5% compared to the industry's 9.5% gain. In the first four months of this year, its Atlantic City casino experienced a slight decline in casino win compared to a market which grew by 8.3%. Through the first three weeks of May, Resorts' win is off 21% from the comparable period a year ago. The casino on Paradise Island, in the Bahamas, now has first class competition from the Crystal Palace Hotel Casino, owned by Carnival Cruise Lines. Our assessment of Resorts' market erosion lies in the fact that their properties are not competitive in their marketplaces. Resorts' casinos need major capital improvements. Mr. Griffin has allocated a budget of \$25 million for each casino. We believe that amounts to a "band aid" approach to a serious problem. Even if the budget were doubled the properties would still not rank as first class facilities.

Meanwhile, the interest rate meter keeps ticking away. This year, Resorts' debt service and principal paybacks total \$133 million. We estimate this year's cash flow at \$60 million. Taking into consideration the capital budget of \$50 million we estimate this year's net cash shortfall will be \$123 million. After the \$325 million junk bond offering late last year, the company set aside over \$125 million in a cash reserve. At March 31, these cash reserves had declined to \$109.7 million. Over the next five years Resorts' debt service and principal repayments range from \$130 million to \$148 million annually.

Another negative for the company is the value of its land holdings in Atlantic City; we think they are worth considerably

less than some previous appraisals. For example, among Resorts' substantial real estate holdings in Atlantic City and the Bahamas lies one of its crown jewels, the 99 year lease on the land on which the Showboat Hotel Casino sits. Showboat currently pays annual rent of \$6.34 million (adjusted to inflation) to Resorts. We have seen appraisals on the value of the lease in a range of \$90-\$100 million. Our estimate falls in a range of \$57 to \$67 million because of the risk factors associated with a casino lease in this environment. Currently, Atlantic City real estate is in a buyers market, and the value of much of Resorts' holdings must be looked at under these circumstances. For over a year we have advised the sale of Resorts International bonds. We would not be enticed by their yields-to-maturity of up to 25%.

**Taj Mahal** - About one block from Resorts stands the uncompleted Taj Mahal, which will be Atlantic City's next new casino. With 4.5 million square feet this facility is huge. About 800 workers are now on the site, to be joined by hundreds more, trying to complete construction by early spring, 1990. When completed, this \$1 billion hotel will have 1,250 rooms and luxury suites, a 120,000 square foot casino, and parking for over 5,000 cars. Its 175,000 square feet of meeting space could qualify the Taj as a mini-convention hall. We are very impressed with the thoughtful planning and quality going into this project. From the standpoint of amenities, this is the kind of property Atlantic City needs for the 1990's. That's when we think the City will be hosting a big convention business and its hotels beginning to reach out beyond their traditional 250 mile radius for customers. From the standpoint of the building itself, we think the Taj makes such a strong statement that it will have a blockbuster opening, especially coming on stream during Atlantic City's busy season.

While we love the esthetics, what scares us about this project is our concern over its financial success. The Taj is going to be a very expensive property to operate, with a \$95 million annual debt service and an annual payroll of \$125 million. We estimate its break-even at about \$1 million a day. It will also have the highest overhead per room of any casino hotel in the world. Its casino will have to win more money per year than any casino in the world in order to operate in the black. While we are not concerned about filling the property during the busy season of 1990 we are concerned about Atlantic City's slow period, from October through January. Adding to our concern is the possible state of the economy in mid to late 1990. A recession could be a big short-term negative for so leveraged a property. Because this is a single use structure, holders of its \$675 million in first mortgage bonds have little to fall back on should the Taj not work. Certainly, it can't be made into a "K Mart".

**Showboat** - The Taj will actually connect to the Showboat, (SBO-\$14) Atlantic City's newest casino. When this 2.1 million square foot facility opened its doors in late March, 1987 it opened to huge

crowds and placed a close second in casino win during its first month of operation. After its big initial month, Showboat lost its momentum and began to trail the first and second tier operators. Last year in a major policy and management change, Showboat went more aggressively after table game players and the result has turned the company into a hot property. For example, in the first four months of this year Showboat's casino win rose by a dramatic 32%, the biggest percentage gain in town. In the first quarter ended March 31, Showboat narrowed its loss to \$2.9 million from the year-ago loss of \$7.7 million. If it can maintain the momentum, we think Showboat's Atlantic City casino will be comfortably in the black in 1989. While management has done a magnificent job in this turnaround, it seems they were not paying as much attention to their casino in downtown Las Vegas. It has been losing market share, and business is down in the double digits. Plans are being formulated to revive this property, too.

**Harrah's Marina** - To get to the beautiful marina area, about two miles northeast of the Boardwalk, we now hop into a jitney and in a few minutes we are in front of Harrah's Marina. After a slow opening in November, 1980 this property has turned into one of the most popular and profitable casinos in Atlantic City. The 2,400 space parking facility has helped build a loyal customer base, especially with down-town-traffic-weary gamblers. Plans are underway to start construction on 1,000 new parking spaces before year end. Harrah's has the loosest slots in town, and as a result its slot win accounts for 60% of its total win. It is no coincidence that Harrah's has the least aggressive bussing program and one of the best operating margins (29.1%) in the business. By catering to the affluent drive-in customer, Harrah's win per square foot is 16% better than average. Best of all, Harrah's has no debt outstanding on its \$281 million investment.

**Trump Castle** - Across the road is Donald Trump's second Atlantic City casino, the Castle. Unfortunately, this is not a model casino, and it has yet to find the correct formula for success. Operating profits are 38% lower than its neighbor, Harrah's. Last year the Castle bussed almost three times as many people to its casino as Harrah's, and this has proven a very expensive way of generating business. The Castle also has the highest ratio of complimentary to revenues among all casinos last year, with the exception of the Atlantis which just closed its doors. From the standpoint of bottom line performance the Castle lost money last year (\$3.1 million) and again in the first quarter of this year (\$2.3 million). Its huge debt of \$324 million was the reason; its interest expenses were a whopping \$41.8 million last year, almost double the industry average and second highest to Resorts International. Mr. Trump, like Bally Manufacturing, seems to find it difficult to market successfully two casinos in the same marketplace. We wish him more luck on his third.

## CONCLUSION

And so we conclude our little tour. As can be seen, all of the casinos offer the same games, but there is a great difference in the way these properties are managed. What is critical to remember is that the bottom line is all important, especially in an environment of debt heavy balance sheets. In the past, many of the operators have ignored the net income line and pointed with pride to their high operating profits. A few operators even felt, that as long as cash flows were sufficient to cover debt service, they were home free. We are raising the red flags. Today's debt loads are in excess of \$2 billion, and they will soon be \$3 billion. Interest expenses of \$293 million last year will jump to \$400 million in 1990. At some casinos there is no longer any leeway for a slow down or a decline in revenues. Big capacity additions, coupled with a slowing economy, could put a few operators over the edge. We have tried to identify the potential problem areas. Investors should be leery of the lure of high yielding junk issues on a number of casinos. We think some properties can literally be a "houses of cards".

Marvin B. Roffman

Additional information relative to the securities mentioned herein is available upon request.

Dow Jones Industrials	(5/30/89)	2493.77
S&P 500 Stock Index	(5/30/89)	321.59

## EARNINGS PROJECTIONS FOR SOME LEADING GAMING COMPANIES

Fiscal Year Ending	Company	Earnings Per Share*			Recent Price	Rating
		1989E	1988	1987		
Dec.	Bally Manufacturing	\$1.60	\$1.12	\$(0.60)	\$25	Hold
July	Caesars, New Jersey	2.35	2.00	1.11	25	Buy
July	Caesars World	3.05	2.89	1.30	36	Buy
Jan.	Circus, Circus	2.50@	2.29@	1.64@	40	Hold
Dec.	Golden Nugget	0.50	(0.33)	0.28	23	Sell
Dec.	Hilton Hotels	2.90	2.72	2.25	82	Sell**
Dec.	Holiday Corp.	1.50A	0.30A	0.02A	48	Sell
Dec.	Pratt Hotel Corp.+	0.05	(0.14)	(0.02)	1	Hold
Dec.	Ramada	0.15	(0.04)	(0.17)	12	Sell
Dec.	Showboat	0.45	(0.37)	(0.32)	14	Hold

\* Earnings per share from operations, excludes extraordinary items.

+ The analyst covering Pratt Hotel has an investment position.

A Excludes gains from hotel sales.

\*\* We rate Hilton a Hold for those who feel a buyout is imminent.

@ Of the following fiscal year.

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