GENERAL ECONOMIC PRINCIPLES AND THE LOTTERY GAMING FACILITY BIDS

A presentation to the State of Kansas Racing and Gaming Commission Review Board

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GENERAL OBSERVATIONS ON THE CONSULTANT REPORTS

- **Review Board has been charged with selecting projects that will**
  - maximize revenues for the State of Kansas
  - enhance tourism and economic development in Kansas or its geographic regions, and
  - be in the best interests of the citizens of Kansas.
- **Consultants' findings and conclusions based on**
  - their experience & expertise
  - descriptions presented in the proposals
  - facts and data drawn from their own research, and
  - the conceptual and empirical models consultants have applied to their analysis
- **Complex issues => Board should ask questions as they come up during Consultant Presentations**

GENERAL ECONOMIC PRINCIPLES AND CASINO INDUSTRIES

- **A high proportion of customers and gaming revenues will come from the local/regional market, within a 100 mile radius of the gaming venues**
- **Distance makes a difference => The closer a customer is to a casino, the greater the aggregate spend per annum at that facility**
- **Casino markets that attract a substantial portion of their clientele from beyond 100 miles usually have significant non-gaming amenities (i.e. outdoor recreation options, scenic attractions, entertainment offerings, or unusual retail, hotel and restaurant outlets.) They also tend to have casino "clusters"**
  - **LV, Reno, Tahoe, Palm Springs, Niagara Falls, Biloxi, Atlantic City**
- **Restricted markets (monopolies) can create substantial profit opportunities that can prevail for relatively long periods**
  - **Certainly the case for Sumner County**

OTHER ECONOMIC FACTORS

- The gaming products found in casinos (slot machines, table games) are highly commoditized
  - Convenience, pricing are the dominant considerations
- The challenge, therefore, is for a casino company to create good reasons for customers to come to their facilities rather than competitors
- Differentiation can occur with ambience, theming, branding, scale, entertainment, non-gaming amenities, loyalty programs, complementary policies, hosting, etc.
- The closer the consumer is to the casino, the more "gaming centric" the consumer is likely to be
  - Non-gaming amenities are more attractive to distant visitors (tourists) than to locals

ECONOMIC AND FISCAL IMPACT ISSUES

- Since local customers are more "gaming centric," they will have only limited impact on businesses outside the casino complex
  - Major economic impacts are more related to employment and increased incomes
- "Net Economic Impact" is the employment and revenue gains from a particular project being developed
  - These come from "exports" and "import substitution"
  - Distinguish from "cannibalization" of other local business, via redirected spending
- Fiscal impacts take into consideration increased demands for public services and infrastructure v. new sources of tax revenues for state and local governments

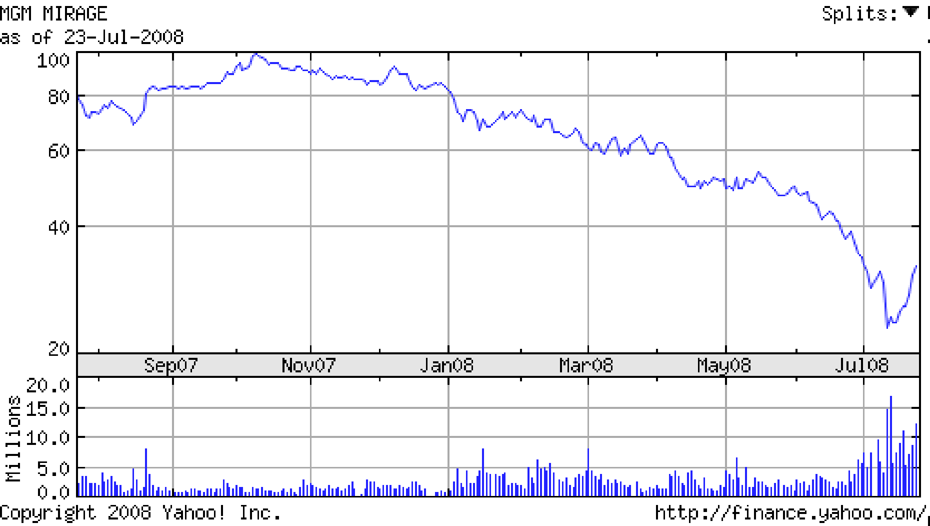
GENERAL ECONOMIC OBSERVATIONS ON THE SOUTHEAST ZONE

- When law was passed, reasonable to build a casino in Southeast Kansas with a CAPEX of $250 m +
- However, Downstream Casino => $300 m+
  - 2,000 slot machines
  - 45 table games
  - 15 poker tables
  - 12 story, 226 room hotel
- Market may not support Downstream, let alone another casino of similar size
  - Merrill Lynch projected $140 m in TR; Wells & Cummings considerably less
  - Kansas casino would have a substantially greater effective tax rate (27% v. 6%)
  - Strategic dilemma for Penn National Cherokee => request “phasing in” to get to their $250 million required CAPEX

GENERAL OBSERVATIONS ON THE GENERAL STATE OF CASINO MARKETS

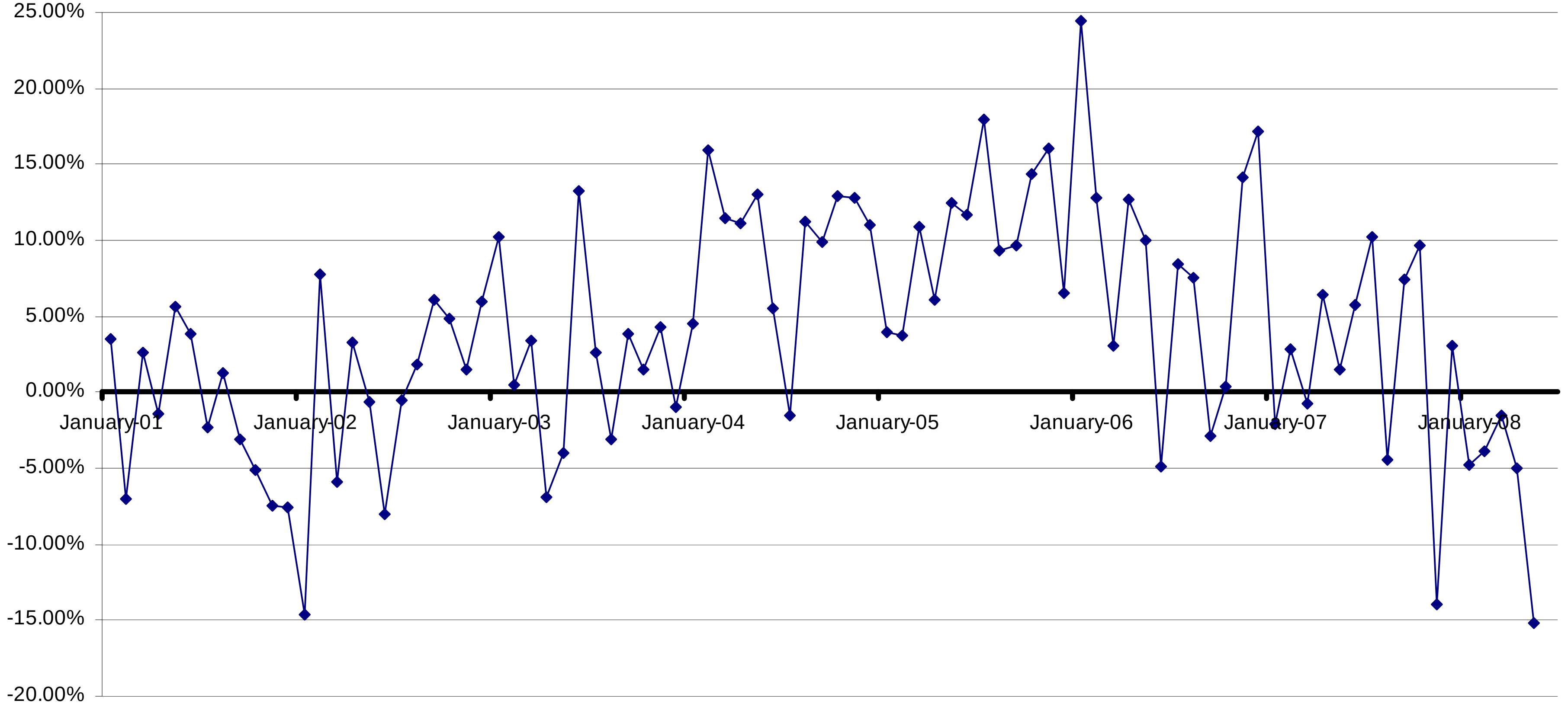
- **Unprecedented increases in gasoline prices and airline ticket prices, as well as increasing food prices**
  - **Family budget constraints are more important than in prior years**
  - **This affects some households much more dramatically than others**
- **Low levels of consumer confidence with respect to the National economic outlook**
  - **Declines for past 6 months; lowest level since 1990**
  - **Consumers in general are going to be more cautious about discretionary spending under such circumstances**
- **Corporations are typically much more cost conscious in recessionary times => Less generous for expense account conventions in Las Vegas or elsewhere**
- **The sub-prime mortgage crisis has adversely affected specific groups in society who are no longer able or willing to participate in the marketplace**
  - **Households who are in, or facing, foreclosure**
  - **Construction workers, realtors, others in financial services**
  - **Others who fear job loss or related cut-backs in income**

STOCK MARKET PRICE TRENDS FOR MGM, WYNN, LVS, BOYD 2007-2008



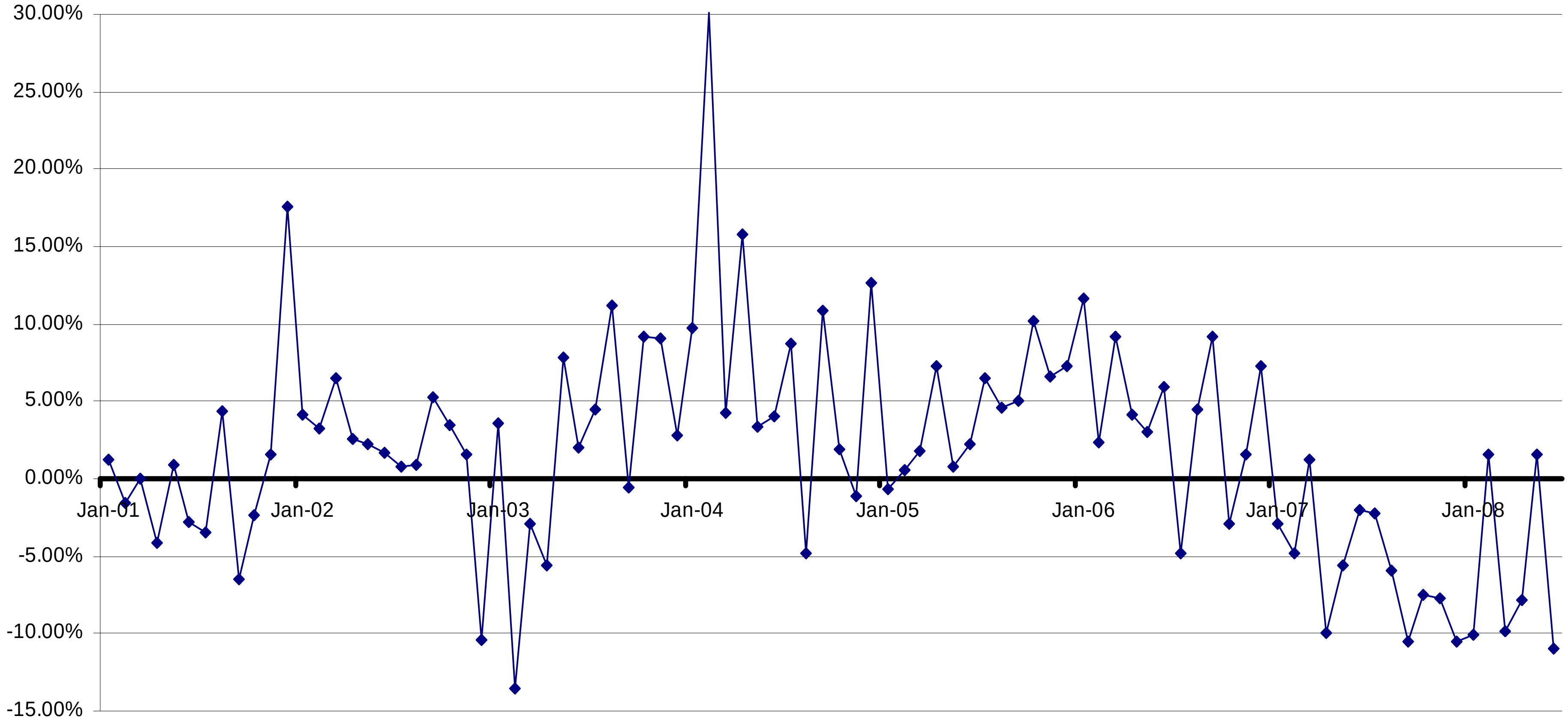
A NUMBER OF MAJOR GAMING STATES ARE BECOMING INCREASINGLY CONCERNED: NEVADA

NEVADA YEAR OVER YEAR GROWTH RATES, SAME MONTH PRIOR YEAR COMPARISONS 2001-2008



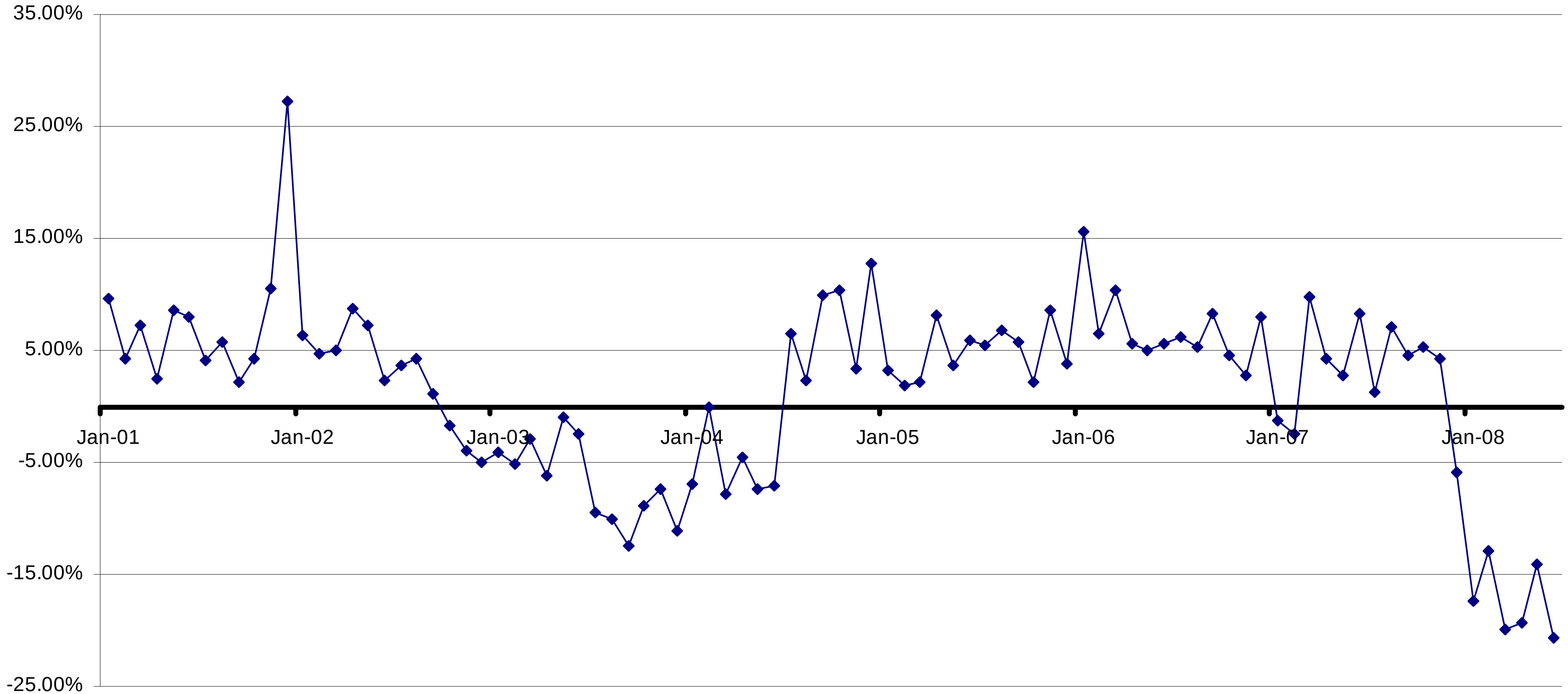
PROBLEMS ELSEWHERE: ATLANTIC CITY

ATLANTIC CITY: YEAR OVER YEAR GROWTH RATE, SAME MONTH PRIOR YEAR COMPARISON 2001-2008



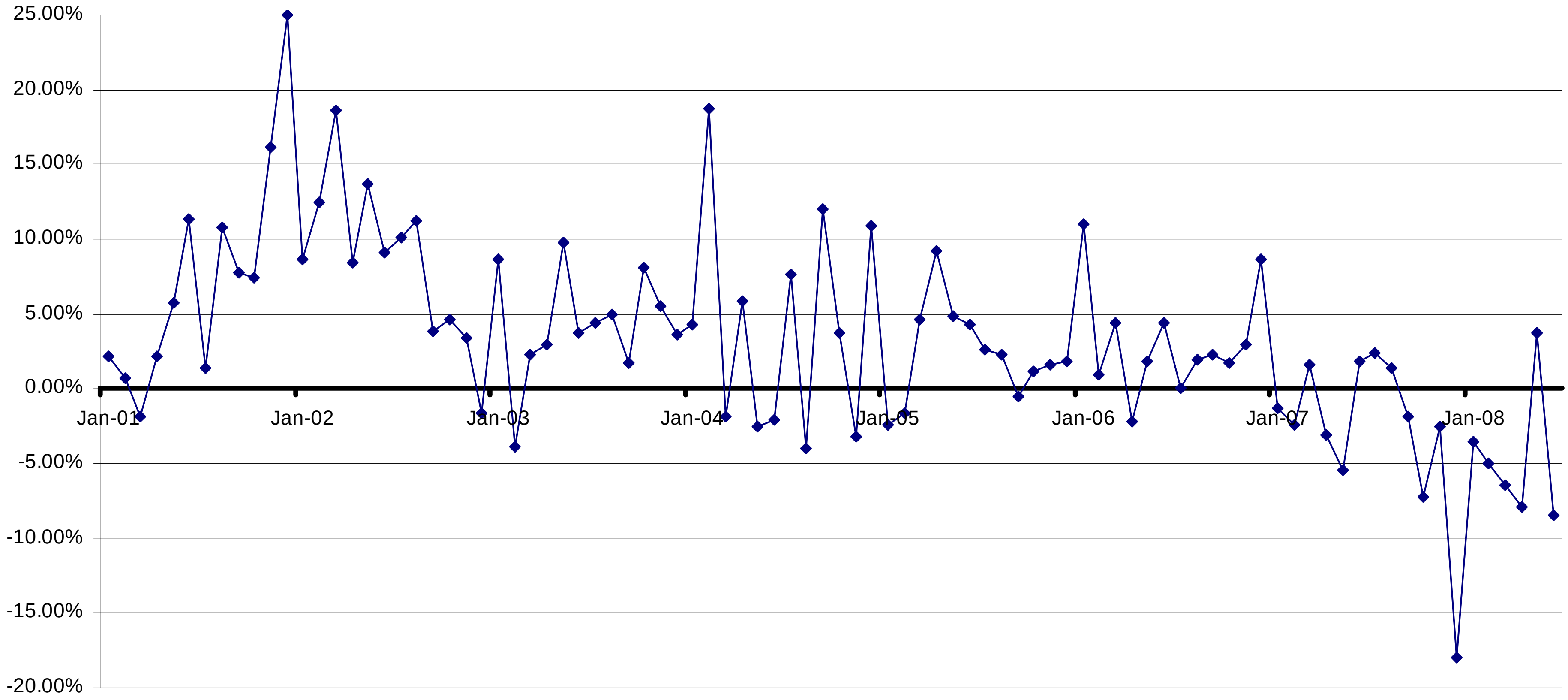
ILLINOIS RIVERBOAT CASINOS

ILLINOIS YEAR OVER YEAR GROWTH RATES, SAME MONTH PRIOR YEAR COMPARISON 2000-2008



CONNECTICUT TRIBAL CASINOS

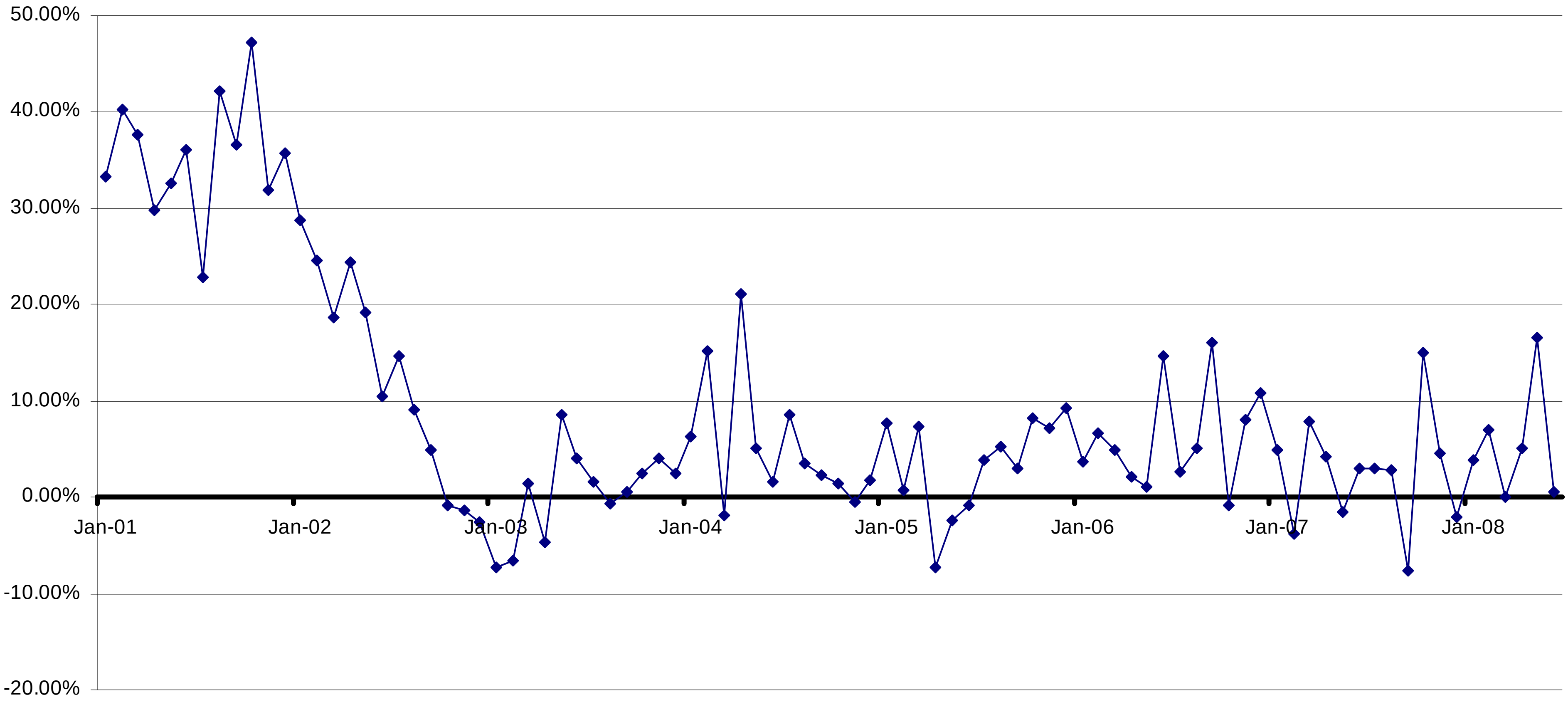
CONNECTICUT TRIBAL CASINOS YEAR OVER YEAR GROWTH, SAME MONTH PRIOR YEAR 2001-2008



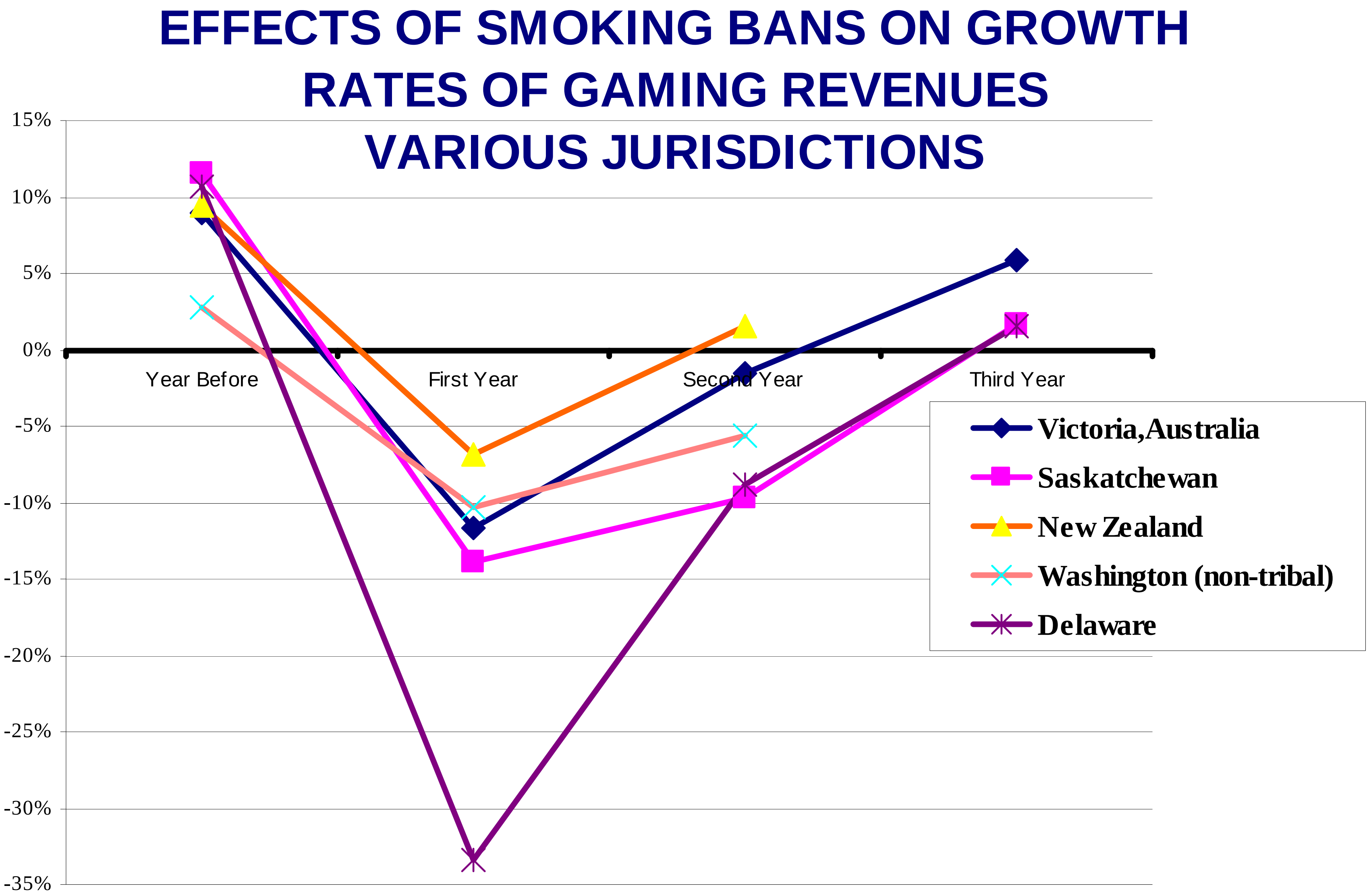
POSSIBLE EXCEPTION: DETROIT

(MGM up 19.0%, or $45 million, for first 6 months of 2008)

MICHIGAN YEAR-OVER-YEAR GROWTH RATE, SAME MONTH PRIOR YEAR COMPARISONS 2001-2008



SMOKING BANS HAVE BEEN SURPRISING IN THEIR IMPACTS



GENERAL ECONOMIC OBSERVATIONS ON THE SOUTH CENTRAL ZONE

- Regional monopoly casino => nearest competing (Oklahoma tribal) casinos will be at least fifty miles away
  - Monopoly profit potential
- Competitive bidding process: proposals try to preserve a portion of the monopoly profits, but with proposed attractions and amenities to gain comparative advantage
  - Challenge is to win the bid without giving up too much profit potential
- Local customers more influenced by gaming offering; tourists will be drawn more by non-gaming amenities
  - What is it about this casino that would make me want to visit it rather than my other choices?

COMPARATIVE STRENGTHS AND WEAKNESSES OF THE COMPETING PROPOSALS

- **Capabilities of the applicants to deliver on their promises**
  - **Financial status**
  - **track record**
  - **Processes and incentives (for customers, employees, management)**
- **What does the applicant really bring to the Zone and the State?**
  - **Brands, player lists, cross-marketing capabilities**
  - **Excuses for locals and tourists to visit their facility**
- **What are the comparative strengths of applicants to attract local visitors? To attract tourist visitors?**
  - **Role of distance; role of non-gaming amenities**