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CHAPTER 22

International Markets

¶ 22.01 Developed vs. Developing Countries 22-2

¶ 22.02 Background for European Countries 22-2
[1] Europe's Legal Framework 22-3
[2] Cultural Differences 22-3
[a] Universalism vs. Particularism 22-3
[b] Affective vs. Neutral 22-4
[c] Sequential vs. Synchronic Time Orientation 22-4

¶ 22.03 The European Countries 22-5
[1] United Kingdom 22-5

EXHIBIT 22-1 Hotel Values Per Room in Euro 1993–1998 22-5

[2] Belgium 22-6
[3] France 22-6
[4] Germany 22-6
[5] Italy 22-6

EXHIBIT 22-2 Average Annual Compounded Growth Rate 1993–1998 (Local Currencies) 22-7

[6] The Netherlands 22-7
[7] Portugal 22-7

EXHIBIT 22-3 Foreign Tourist Arrivals to Italy and other Key European Countries (1994–98) 22-8

EXHIBIT 22-4 Hotel Values–% Change in local currencies 22-9

[8] Spain 22-9
[9] Central and Eastern Europe 22-9
[a] The Czech Republic 22-10
[b] Hungary 22-10
[c] Poland 22-11
[d] Russia 22-11

¶ 22.04 Middle East and North Africa 22-12
[1] Overview 22-12
[2] Obstacles to Increased Tourism 22-12

EXHIBIT 22-5 Regional Tourism Trends 1989–1998 22-13

EXHIBIT 22-6 Top Destinations World-Wide . . . 22-13

EXHIBIT 22-7 Occupancy %—Point Change 1997–1998 22-14

[3] Hotel Data 22-14

EXHIBIT 22-8 Regional Tourism Trends 1989–1998 22-14

EXHIBIT 22-9 Average Room Rate—% Change 1997–1998 22-15

EXHIBIT 22-10 RevPAR—% Change 1997–1998 22-15

EXHIBIT 22-11 Current and Future Supply 22-16

¶ 22.05 Countries of the Middle East and North Africa 22-16
[1] Bahrain 22-16
[2] Egypt 22-17
[3] Israel 22-18
[4] Jordan 22-18
[5] Kuwait 22-19
[6] Lebanon 22-19
[7] Morocco 22-20
[8] Oman 22-20
[9] Palestinian Areas 22-21
[10] Qatar 22-21
[11] Saudi Arabia 22-22
[12] Syria 22-22
[13] Tunisia 22-22
[14] United Arab Emirates 22-23
[15] Yemen 22-23

¶ 22.06 Asian Markets Values 22-24

EXHIBIT 22-12 Asian HVI in US$ Ranked by index in 1997 22-24

EXHIBIT 22-13 Hotel Values per Room in US$ Ranked by Value in 1997 22-25

[2] Hotel Values 1998 22-25

EXHIBIT 22-14 Value per Room Comparison in US$ (December 1997 and July 1998) 22-26

EXHIBIT 22-15 Percentage Change from Peak Value 22-26

¶ 22.07 The Asian Countries 22-27
[1] Jakarta and Bali, Indonesia 22-27
[2] Hong Kong 22-27
[3] Beijing and Shanghai, PR of China 22-27
[4] Kuala Lumpur, Malaysia 22-28
[5] Mumbai, India 22-28
[6] Seoul, South Korea 22-28
[7] Tokyo, Japan 22-28
[8] Singapore 22-29
[9] Manila, Philippines 22-29
[10] Bangkok, Thailand 22-29

» 22.01 DEVELOPED VS. DEVELOPING COUNTRIES

Countries with rapid development offer more opportunities to the investor than those with slower growing economies. At the same time, there is a great deal more risk— political and financial—associated with a rapidly expanding economy. One way of overcoming this risk is to deal in assets that are easily salable, thus allowing the rapid conversion to currency that can be withdrawn from the market. Such investments also allow a level of hedging to be used as a fallback against risk in the marketplace.

Unfortunately, hotels are large static assets with high capital costs and poor conversion abilities. In addition, hotels are not easily transferred among investors, which means that the hotel owner is exposed to risk on an ongoing basis; every time the operation is exposed to market uncertainty, the capital value of the operation is affected. For these reasons, an investor should be very careful about entering a developing market.

Return, however, is a function of risk; while a hotel in a developed market is a more stable investment, it will not yield the return that is possible in a developing marketplace.

» 22.02 BACKGROUND FOR EUROPEAN COUNTRIES

If a firm is to control its development and grow in international markets, it is important that it pay attention to what are known as "environmental factors." These are as follows:

- *The economy.* The overall strength of a country's economy affects the availability of credit, the willingness of people to borrow, and, ultimately, the level of demand. Interest rates and currency fluctuations affect both the cost of and the demand for imports and exports.
- *Capital markets.* The state of capital markets in the country invested in has a direct bearing on the cost and availability of loan capital. It also reflects and influences the willingness of investors within the country to invest in internal markets rather than overseas. Capital markets have been shown to have a great effect on the economy as a whole.
- *Government.* The governments of many countries seek to encourage foreign investment through the allocation of grants and industry initiatives. Also crucial is the degree of government regulation of the economy. Political decisions made either internally or on an international scale can have devastating effects within the hotel industry.
- *Labor markets.* The availability of labor and skill bases is crucial and must be investigated.
- *Suppliers.* In third world and developing countries, maintaining the supply of raw materials for construction, refurbishment, and everyday running stock is an enormous challenge, one that is to a large extent nonexistent in a developed country.
- *Markets.* The influence of local and international tourism markets and the presence of competitors must be taken into account.

This chapter will begin with a discussion of the markets of Europe.

[1] Europe's Legal Framework

International legal practice in Europe is mostly carried out through branch offices, alliances, informal associations, referral relationships, and foreign lawyer employment. On the whole, lawyers are a vital part of European real property transactions as technical facilitators. In the United Kingdom, for example the solicitors' profession still has a statutory monopoly on conveyance work. This has been challenged in recent years and will change, albeit slowly. The legal framework in Europe has been complicated somewhat in recent years by the application of European Community (EC) laws and directives, which have challenged bodies of law in individual countries.

Because there is nothing in the EC treaty that creates any EC function or power relating to the ownership or transfer of land, the national laws of each member state govern those matters. However, certain aspects of real property transactions may be affected incidentally by provisions of the EC treaty.

The major common-law jurisdictions of Europe are England, Wales, Scotland, Northern Ireland and the republic of Ireland, while the remaining jurisdictions are essentially civil law systems. The systems vary principally in their approach to case law. In both groups legislation plays an increasing role in the regulation of real estate matters, both in the private aspects of ownership and transfer and in the public aspects of planning, building controls, and more general environmental concerns. However, the traditions of statutory interpretation also vary' considerably between the two regimes.

The land tenure system originated in private law, according to the doctrine of binding precedent and with substantial contribution from professional practice. Legislation has introduced important measures such as registration of title and reform of old case law. It has also intervened to provide important rights (e.g., rent control for residential tenants and lease renewal rights for business tenants) and to impose planning and environmental controls of increasing complexity.

The status of court decisions in relation to civil law is quite different than under common law. Legislation has increasingly replaced or reformed original code provisions or enacted controls not included in the original codes. The planning, building, and development policies of individual European countries are discussed subsequently in this chapter.

The EC has an increasingly positive attitude towards foreign investment. Most countries make no distinction between foreign and domestic investors, though in certain sectors and in certain countries restrictions remain. For example, foreign investment in France is restricted in banking and insurance. In Spain it is restricted in the gas, water, electric, and railway industries. The state-controlled industries of Italy are restricted. For the most part, however, countries use attractive incentive packages to encourage investment.

[2] Cultural Differences

The following section offers generalizations about some of the cultural differences found in the international markets as an aid to understanding how to conduct business there. The categorizations outlined are the product of the research of Fons Trope-naars of the Centre for International Business Studies (CIBS).

[a] Universalism vs. Particularism

This is essentially the difference between rules and relationships. Universalist behavior or rule-based behavior focuses on the rules governing the conduct of areas of be-

havior. The belief of people in a universalist society is that all should be treated equally under the law and that people should adhere to the regulations and rules laid out by the society they live in. Particularists, in contrast, see rules as applying in certain circumstances and not in others. Particularists will choose whether to adhere to the rules or not depending on the situation they find themselves in. Universalist countries include the USA, Switzerland, Sweden, Norway, Germany, Britain, the Netherlands, Denmark, Finland, and Austria. Particularist societies include Russia, Hungary, Bulgaria, Romania, Greece, Spain, France, Portugal, Oman, and Egypt.

Particularist countries put more faith in personal relationships, and as a result, more time is often needed to conduct business; they also see the universalist need for contracts and high powered negotiations as suspect. Universalists, on the other hand, might see the time it takes to establish these relationships as a waste of time and a sign of a lack of commitment. For this reason, this cultural difference can lead to misunderstandings. The following lists summarize the differences between the two categories.

For universalists:

1. Focus is more on rules than on relationships;
2. Legal contracts are not subject to easy change;
3. Trust is based on the honoring of a contract; and
4. A deal is a deal.

For particularists:

1. Focus is more on relationships more than on rules;
2. Legal contracts can be readily modified;
3. Trust comes from establishing worthiness over time; and
4. Relationships evolve.

[b] Affective vs. Neutral

Affective cultures are those that show their emotions, whereas neutral societies are those that do not willingly show their emotions. This does not mean, of course, that those cultures that do not seek outlets for their emotions are devoid of emotion; in most cases, it is simply a matter of social convention. There are considerable differences in this regard among European countries, with Germany being the most neutral and Italy and France being the most affective. The differences have a great influence on the way relationships are formed and communication occurs within these different cultures.

Neutral and affective cultures often find each other immensely confusing in a business context. This confusion can lead to difficult problems in negotiations.

[c] Sequential vs. Synchronic Time Orientation

How different cultures view time is a very important aspect to doing business. In hotel development terms, it becomes all the more crucial, because the development process is a lengthy one that requires a great deal of coordination of resources. Sequential cultures such as the United Kingdom and the United States of America tend to run "on time" with attention paid to appointment times. In such cultures, people set specific goals and wish to complete one task before embarking on the next.

Synchronic cultures, such as the southern European countries, often prefer to do more than one thing at a time. They are less goal-specific and see time as an indicator of direction and not a controller of action.

» 22.03 THE EUROPEAN COUNTRIES

[1] United Kingdom

The United Kingdom hotel market remains strong with operating performances for both London and the provinces continuing to lead their European counterparts. Average occupancy levels declined slightly in the capital but the Provinces enjoyed a marginal increase, while average room rates for the United Kingdom increased by approximately 9% across the board. The branded budget sector continues to grow throughout the country, especially in city center locations, causing increasing concern from independent hotel owners. The strength of the market has continued to motivate sales activity and development from both domestic and foreign investors.

Some felt at the beginning of 1998 that London in particular was nearing the peak in the cycle, and yet transaction activity continued steadily throughout the year. Exhibit 22-1 shows that London hotels still lead Europe in Value per room.

Exhibit 22-1 Hotel Values Per Room in Euro 1993-1998

Source: HVS International

	1993	1994	1995	1996	1997	1998
London	245,617	276,810	293,330	358,743	496,007	504,990
Paris	360,262	352,336	340,709	316,953	389,947	433,515
Geneva	234,149	250,549	272,657	265,541	267,766	279,867
Zurich	204,242	220,064	221,492	211,042	236,044	267,574
Rome	155,319	170,562	160,459	205,974	238,614	264,487
Amsterdam	122,574	130,897	145,949	170,177	192,981	213,762
Madrid	149,874	142,183	142,416	161,663	188,540	209,076
Europe	145,812	147,066	149,256	162,042	190,528	204,202
Barcelona	85,399	78, 074	84,504	110,015	141,299	172,308
Istanbul	100,258	100,896	96,454	123,435	165,709	165,276
Vienna	153,557	144,497	150,496	145,934	141,970	157,959
Brussels	121,886	115,376	120,223	127,017	143,492	155,594
Stockholm	87,589	94,355	103,986	136,182	150,744	153,216
Copenhagen	97,643	105,259	109,116	124,337	144,450	150,920
Budapest	86,012	91,683	82,204	97,733	143,425	147,349
Warsaw	121,855	108,790	108,499	124,157	144,352	147,349
Frankfurt	136,758	134,160	137,916	130,606	137,920	141,829
Prague	129,487	110,150	104,350	111,747	134,533	136,485
Lisbon	102,966	98,029	95,877	108,879	112,256	127,098
Athens	86,393	84,405	84,627	96,554	113,645	126,896
Berlin	134,394	132,243	129,863	114,150	126,866	126,796

[2] Belgium

The recovery of the Belgium hotel market, in terms of occupancy and average room rates, has led to increased interest from investors. Brussels still lags the European average for hotel valuation (Exhibit 22-1), despite improved hotel conditions.

[3] France

The market recovery enjoyed by the French hotel market in 1997 was sustained in 1998. Continued growth in occupancy levels was enjoyed, in particular, in provincial cities, such as Marseilles and Paris, which hosted some of the 1998 football World Cup games. The month of June saw occupancy levels soar to new heights in certain cities due to the estimated half a million visitors for the games. There were concerns that the World Cup events would deter traditional demand from the leisure and commercial sectors and that this would have a negative impact on occupancy levels. These concerns proved to be unfounded in cities situated in the north of France; however, particularly in the southern regions, others did report a decrease in domestic leisure and commercial demand. The strengthening of the French economy and the strong US dollar, British pound and Italian lira have also contributed to some of the growth in demand for hotel accommodation. Paris was the principal beneficiary of the strengthening of the French market, enjoying strong growth in both rooms occupancy and average room rate. Paris hotel values remain strong and are second only to London (see Exhibit 22-1).

[4] Germany

The German hotel market still seems to be suffering from the economic recession of the early 1990s. The hotel construction boom continues in Germany between May 1997 and April 1998, 80 new hotels with almost 14,000 rooms were constructed throughout the country. A further 140 hotels with over 37,000 rooms are planned over the next three years. New hotels are particularly prevalent in Berlin, with fewer than 64 hotels planned or under construction. Berlin is the only major European city to actually have its value decrease between the years 1993-1998 (See Exhibit 22-2, Average Annual Compounded Growth Rate 1993-1998). Although performance has been low in 1998, hopes are high for the future. For Berlin, in particular, an increase in demand is expected with the relocation of the German government from Bonn to Berlin and the arrival of 12,000 civil servants. Frankfurt is also one to watch as it capitalizes on being home to the Euro.

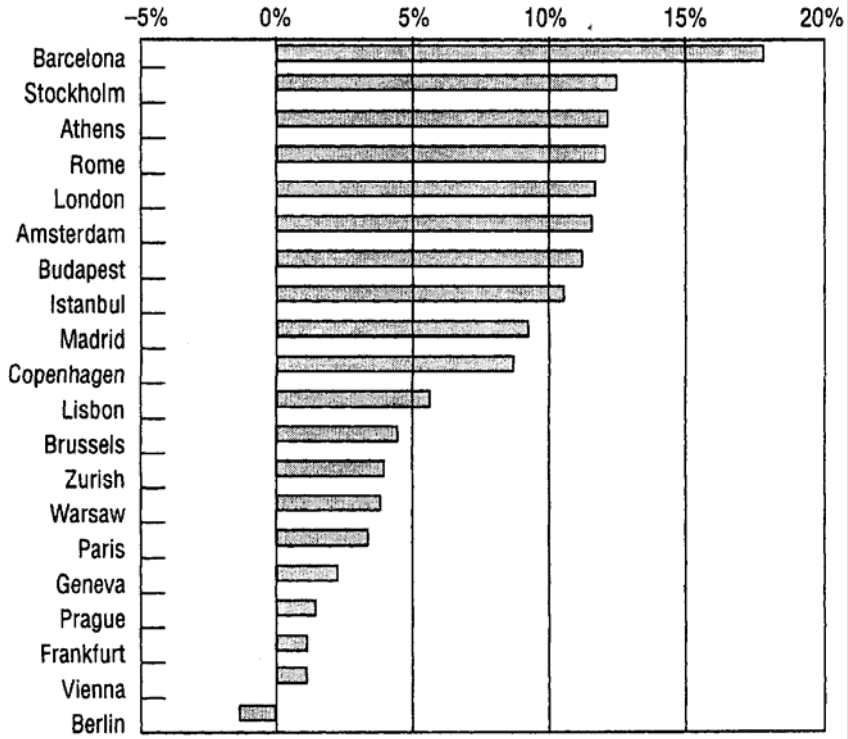
[5] Italy

The Italian hotel market is the largest in Europe in terms of the number of hotel rooms; Italian tourism is second in the world (behind the USA) in terms of receipts. It is also the fastest growing in terms of foreign tourist visits between the years 1994-1998 (see Exhibit 22-3).

In the last 24 months, the national government appears to have achieved notable success in stabilizing Italy's economy and developing a level of confidence among domestic and foreign investors. The current Ulizo coalition has continued to work off its most recent predecessors, to drive Italy into the European Market Union, although this has been at the cost of stern monetary and fiscal control of the economy.

Exhibit 22-2 Average Annual Compounded Growth Rate 1993–1998 (Local Currencies)

Source: HVS International



[6] The Netherlands

The Netherlands has suffered for years from an abundant supply of hotel rooms for several years. It has finally worked off this excess room supply and values have increased dramatically in the few years (See Exhibit 22-4). The average has increased from below the European average in 1993 to well above average by 1998.

[7] Portugal

After suffering from a prolonged recession in recent years, the Lisbon hotel market enjoyed buoyant performance during 1998, largely due to the hosting of Expo '98. RevPar in five-star hotels improved by up to 40% compared with the 1997 performance, which was mainly driven by average rate growth. Occupancy grew by approximately 10%, despite Lisbon's hotel market being subject to a huge increase in supply in all categories compared to 1997.

It is envisaged that the hotel supply in and around Lisbon will increase by 12% in 1999, which includes a 150-room Marriott golf resort hotel situated one hour's drive of the city. Demand for new hotels in other regions of Portugal such as the Algarve is also set to increase in 1999. This is partly as a result of improved infrastructure, a prime example being the recently modernized and enlarged Lisbon Portela Airport, but also as a result of key European source markets that are benefiting from favorable economic conditions.

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Exhibit 22-3 Foreign Tourist Arrivals to Italy and Other Key European Countries (1994-98)

Source: WTO

Rank	Foreign Tourist Arrivals to:	1994	1995	1996	1997	1998	1998 as a % of Total	% Growth 1994-98
1	France	61,312,000	60,033,000	62,406,000	66,864,000	70,000,000	32%	14%
2	Spain	43,232,000	39,324,000	40,541,000	43,403,000	47,743,000	22	10
3	Italy	27,480,000	31,052,000	32,853,000	34,087,000	34,829,000	16	27
4	UK	20,794,000	23,537,000	25,163,000	25,515,000	25,475,000	12	23
5	Germany	14,494,000	14,847,000	15,205,000	15,837,000	16,504,000	8	14
6	Switzerland	12,200,000	11,500,000	10,600,000	10,600,000	11,025,000	5	-10
7	Netherlands	6,178,000	6,574,000	6,580,000	6,674,000	6,170,000	3	0
8	Belgium	5,309,000	5,560,000	5,829,000	6,037,000	6,152,000	3	16
	Total Foreign Tourist Arrivals	**190,999,000**	**192,427,000**	**199,177,000**	**209,017,000**	**217,898,000**	**100%**	**9%**

Exhibit 22-4 Hotel Values—% Change in local currency

Source: HVS International

	1994	1995	1996	1997	1998	1994-1998
Barcelona	-1.8%	14.0%	25.7%	29.4%	22.6%	123.2%
Athens	5.6	8.3	13.6	17.7	16.6	78.3
Zurich	1.6	-1.5	-5.1	10.8	14.8	20.8
Lisbon	0.2	0.1	11.5	2.6	13,4	30.2
Stockholm	9.1	15.3	17.4	9.0	12.5	81.1
Vienna	-5.9	4.3	-3,0	-3.3	11.8	2.9
Rome	14.9	7.8	15.0	11,6	11.6	77.5
Madrid	1.9	5.5	9.6	17.5	11.5	54.3
Amsterdam	6.6	11.4	16.6	13.4	11.4	75.0
Paris	-2.2	-3.3	-8.6	22.3	11.3	17.7
Europe	1.5	6.2	7.7	12.0	9.1	41.8
Brussels	-6.7	4.1	5.6	13.3	8.4	26.0
Budapest	8,6	1.6	13.3	27.2	8.3	72.2
Warsaw	-9.1	13.0	9.1	0.8	6.4	20.2
Geneva	0.9	6.5	-3,2	0,1	5.9	10.2
Prague	-13,4	7.3	2.1	4.4	5.7	4.8
Copenhagen	7.8	3.4	12.2	15.0	4.8	50.7
Istanbul	2.5	8.3	22.0	16.4	3.9	63.9
Frankfurt	-1.9	2.8	-5.3	5.6	2.8	3.7
Berlin	-1.6	-1.8	-12.1	11.1	-0.1	-5.7
London	12.7	16.8	16.6	15.3	-1.0	75,2

[8] Spain

Spain has shown very little growth in recent years as hotel building has slowed dramatically. However, recently international hotel operators and entrepreneurial investors alike have been talking about Spain as a likely growth area, despite its slow hotel growth rate.

[9] Central and Eastern Europe

After the collapse of communism in the period 1989-1990, investors became very interested in Central and Eastern Europe. Still, because of the recession there was not much development. Interest rates were high, and there was a squeeze on the availability of development finance. Another reason for the lack of development in these nations is their considerable political uncertainty. However, the Czech Republic, Hungry and Poland have stabilized their political structures as well their economics. With the three above mentioned counties joining NATO, the outlook for the future development of hotel projects will be carried out in a stable environment. Russia is still experiencing great difficulty economically and is still considered an extremely risky hotel development opportunity.

However, with the advent of free market economies in the Czech Republic, Hungry and Poland there has been a rush to build properties and create a short term overbuilt market. In fact the hotel valuation for the major cities in these counties has performed below the European average in 1998 compared to 1997 (See Exhibit 22-4, Hotel Values - % Change).

[a] The Czech Republic

The Czech Republic has come a long way during the past three years, with GDP growth estimated at 4.2 percent for 1995. An important reason for this growth is the entrance of the Republic into the world trade market, as reflected by a 20 percent to 30 percent increase per year during the past three years in export growth. The willingness to trade, coupled with rising consumer demand, has resulted in increased imports and, ultimately, economic expansion. In contrast to many of its neighbors, unemployment in the Czech Republic is relatively low, at 3.2 percent for 1994 and an estimated 3.5 percent in 1995. Inflation has also been kept in check, quite a feat in light of the rapid expansion of the economy and the huge capital inflows to the country. Interest rates are still high compared with the rest of Europe, but they are in line with neighboring countries and could be said to be reasonably low considering the present economic status of the country. The next few years should bring no real slowdown to the economy, and if inflation can be kept in check, the future prospect looks favorable.

Prague probably will become one of the main centers for hotel development in Central Europe. There are numerous hotel projects under construction in the capital, and there is interest from other major international chains. The following hotels can now be found in the Republic: the Ramada Renaissance, the Grand Hotel Bohemia, and the Savoy, with Hilton taking over the management of the Atrium hotel in 1995. However, the current climate is one of rising costs and low average rates, which are not the best conditions for new hotels. Still, those hotels already in place will achieve good returns when this trend reverses in the near future. The country still has many interesting investment opportunities, which will no doubt be enhanced by the AAA rating given by Standard and Poor's. Investment in development projects has continued to be led by Austrian banks such as Raiffeisen and Girocredit, and Munich-based Hypobank has also become involved in the development of some prime real estate sites. The French institution Caisse des Depots has also been heavily involved in the market. ING has announced plans to become involved in the development of various large-scale projects in the area. On the whole, European investors have lower yield expectations than those of their U.S. counterparts; considering the state of the economy and the length of time it will take to mature, companies accepting lower yields in the interim will be in a better strategic position than the late entrants.

[b] Hungary

The Hungarian economy has slowed slightly, down from 2.9 percent GDP growth in 1994 to close to 2.0 percent growth in 1995. The reason for this was the government's austerity package, designed to implement needed economic reform. The reform dampened the still buoyant export performance as well as the country's relatively strong internal consumer demand. Meanwhile, privatization is making slow but steady progress, with small to medium-sized companies being established in all market sectors. Inflation remains high at 28.3 percent for 1995, despite the monetary controls imposed by the government. This figure appears ready to drop in 1996 and 1997, however, as the economy absorbs the impact of the economic reform. Employment is still high, at 10.3 percent, but it is forecast to stabilize at about 10 percent. The effects of the increase

have been offset in part by the high level of imports and inward capital flows required by the restructuring process.

Strong performance in the Budapest market between 1989 and 1992 was followed by poor market performance in 1993, as the initial "novelty travel" declined. In 1994, the market sector picked up again, as a result of increased political and economic stability and the implementation of the government's privatization program. In 1995, occupancy levels were stable, and there was moderate growth in average rates. There has been little new development in the marketplace recently, and the cancellation of the 1996 World EXPO will dampen prospects in the market. The Austrian bank Girocredit has been heavily involved in the marketplace, with German, Dutch, and French banks also entering the market on a lesser scale. The problems facing prospective investors in the Hungarian market are many and mainly bureaucratic. Another major obstacle seems to be the lack of suitable investment property—many of the prime locations are already owned by investors who are seeing a good return and therefore are under no pressure to sell. Another problem is that the values of much of the real estate are based on an "initial yield attainable" basis, which does not help those who would choose to value on a revisionary basis. Yields in other industrial sectors are currently running from 12 percent to 14 percent, though this should increase in 1996 as the first round of rent reviews take place. In January 1996, the Hungarian Insurance law was revised, bringing the regulatory environment closer to EU thinking on issues such as minimum capital requirements. This should increase the stability of the financial markets.

[c] Poland

The Polish economy recorded yet another year of impressive economic expansion in 1995, with GDP growth of close to 5.7 percent, up from 5 percent the previous year. This was by far the best performing economy of the former Eastern bloc countries. There has been increased foreign direct investment in the country. The government is committed to a structural reform of the economy and is pursuing an almost egalitarian transition to free market economics. While unemployment is high, the economy on the whole is on sound footing.

Another reason for the lack of development in these nations is their considerable political uncertainty and lack of basic infrastructure. Warsaw hotels have declined markedly in performance since 1991, as the market has struggled to absorb the plethora of new hotel developments in the city. Occupancy rates, which stood at 70 percent in 1991, fell to 50 percent in 1993. In 1995, the occupancy rates improved, but average rates suffered. While there are a number of proposed new hotels, it is doubtful that they will be built until there is an increase in demand.

[d] Russia

Russia has had perhaps the hardest time of the previously communist countries in developing a free market economy. This can be explained to an extent by its sheer size, which has led to a much greater level of economic mobilization. It has suffered countless setbacks in the last few years from political instability and large-scale upheaval. Despite all this, Russia has moved steadily toward attaining a market economy; in 1995, it reduced the contraction of the economy to -4 percent GDP growth—a large improvement on the previous year's -15 percent. Exports increased in 1995, helped in part by progress made with the government's privatization program. There has been a large decrease in the rate of inflation in the country, from 843 percent in 1993 to 131 percent in 1995 to a projected 25 percent in 1996. Although this will undoubtedly help the economy, it is a long way from offering the security needed by investors, especially when the currency continues to devalue. The restructuring in the

economy has had the unfortunate effect of increasing unemployment, which has contributed to the general feeling of unrest in the country. In the key cites in Russia, areas in which the first major investments are being made, there is increasing concern about the rise in Mafia-style business tactics and profiteering, which is making the country a high-risk area for new business ventures.

Most of the major development taking place in Russia at present is taking place in Moscow or St Petersburg. In Moscow, the major hotel developments have occurred after 1990, with the notable exceptions of the Savoy, the Metropole, and the National. There is huge potential for development in these two markets, and this has been supported by the rapid absorption of all the new hotels to have opened in the last few years. Between 1991 and 1993, the number of rooms in Moscow increased by 150 percent, with little effect on either occupancy or average rate. In 1995, four- and five-star hotels sustained an average rate in excess of $230 (U.S. dollars) and an occupancy rate of close to 68 percent. There are a large number of projects on the drawing board at the moment, and the marketplace looks set for a great deal of development during the next few years.

The investment market in Russia is still relatively underdeveloped. It is still very difficult to purchase property in Russia except through the vehicle of a Russian-owned company, and there is extensive and unclear legislation concerning the transfer of title over land. There is also the continuing risk of reappropriation of property, as the nation's commitment to capitalism is far from secure. The financial sector is still in disarray, suffering from both a lack of knowledge and high local financing costs. The number of banks being created is only just capable of keeping up with the number that are going into liquidation. It is almost impossible to ascertain the current yields being achieved by property investments in Moscow and St Petersburg—as there is little if no information available—some estimates put the range between 13 percent and 20 percent.

» 22.04 MIDDLE EAST AND NORTH AFRICA

[1] Overview

Prior to the 1970s, tourism demand in the Middle East was virtually nonexistent. The development of tourism facilities, primarily hotels, occurred in the late 1970s and the early 1980s, partly in response to demand from international travelers looking to capitalize on the wealth generated from oil production. Today, tourism in the region is a small but rapidly growing industry.

Regional tourism trends show that the Middle East and Africa have experienced above average growth rates compared to the rest of the world (see Exhibit 22-5, Regional Tourism Trends). However, the total increase in the number of visitors to the Middle East and Africa is only 18 million or 9 % of the total tourist increase in the years 1989-1998. In fact, of the top destinations in the world only Tunisia, Egypt, and Saudi Arabia rank in the top 35 (see Exhibit 22-6, Top Destinations World Wide).

[2] Obstacles to Increased Tourism

Political instability in the Middle East and North Africa is the major obstacle to increased tourism. Tensions between the State of Israel and its Arab neighbors alone have resulted in numerous conflicts since 1948. Difficulties have arisen between Arab countries—for

example, the Iran/Iraq war and Iraq's invasion of Kuwait in 1990. In almost all Middle Eastern countries there is some type of conflict either above or just below the surface. It will not be until these tensions are finally eradicated that the industry will flourish.

Exhibit 22-5 Regional Tourism Trends 1989-1998

Source: WTO

	Increase in Arrivals		Average Annual Growth Rate	
Region	**1989-1998 (millions)**	**1989-93**	**1994-98**	**1989-98**
Africa	11.1	7.6%	6.9%	6.8%
Americas	33.2	4.5%	3.1%	3.7%
East Asia/Pacific	39.2	10.5%	3.1%	6.9%
Europe	106.2	3.9%	3.0%	3,8%
South Asia	2.0	3.7%	7.0%	5.9%
Middle East	7.1	7.4%	5.1%	6.9%
WORLD	198.8	5.0%	3.2%	4.3%

Exhibit 22-6 Top Destinations Worldwide

Source: HVS International

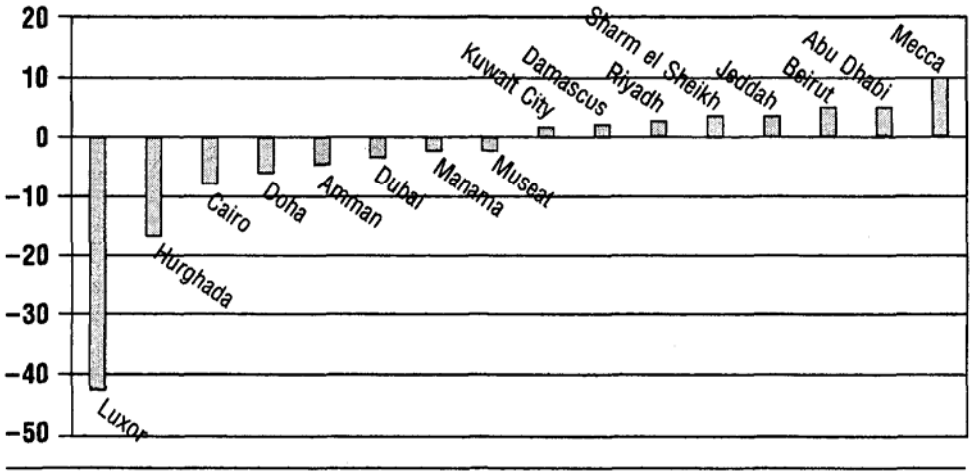
Rank	Country	Arrivals (OOOs)	%0f Total	Rank	Country	Arrivals (OOOs)	%0f Total
1	France	70,000	11.2%	11	Germany	16,504	2.6%
2	Spain	47,743	7.6%	12	Czech Republic	16,325	2.6%
3	United States	47,127	7.5%	13	Russian Federation	15,810	2.5%
4	Italy	34,829	5.6%	14	Hungary	14,660	2,3%
5	United Kingdom	25,475	4.1%	15	Portugal	11,800	1.9%
6	China	24,000	3.8%	16	Greece	11,077	1.8%
7	Mexico	19,300	3,1%	17	Switzerland	11,025	1.8%
8	Poland	18,820	3.0%	18	Hong Kong	9,600	1.5%
9	Canada	18,659	3,0%	19	Turkey	9,200	1.5%
1	Austria	17,282	2.8%	20	Thailand	7,720	1.2%

Rank	Country	Arrivals (OOOs)	%0f Total
29	Tunisia	4,700	0.8%
34	Egypt	3,766	0.6%
35	Saudi Arabia	3,700	0.6%

Religious fundamentalism still represents a major problem for the political and economic stability of the region and for the tourism industry in particular. The threat of fundamentalism is most acute in Egypt and Algeria. The terrorist attack at Luxor in the 1990s has devastated the tourism industry in Egypt, with occupancy at Luxor dropping over 40% between 1997 and 1998 (see Exhibit 2-7, Occupancy % Change).

Exhibit 22-7 Occupancy %—Point Change 1997–1998

Source: HVS International



[3] Hotel Data

After significant growth after 1994, tourism receipts have leveled off until 1998 (see Exhibit 22-8, Regional Tourism Trends). However, as previously noted the increase has not been even across the board, with the Luxor and Cairo showing large decline in occupancy percent and Mecca showing the largest increase occupancy as a result of decreased tensions with its Arab neighbors.

Exhibit 22-8 Regional Tourism Trends 1989-1998

Source: WTO

	Increase in Receipts		Average Annual Growth Rate	
Region	**1989-1998 (US$ bn)**	**1989-93**	**1994-98**	**1989-98**
Africa	5.1	8,8%	8.5%	8.7%
Americas	61.1	10.9%	6.2%	8.1%
East Asia/Pacific	39.5	12.0%	3.8%	8.9%
Europe	110.2	9.2%	6.0%	7.7%
South Asia	2.4	7.9%	9.4%	9.3%
Middle East	5.2	6.1%	11.0%	8.9%
WORLD	223.5	10.0%	5.9%	8.1%

1998 has shown that most cities in the Middle East have had a significant drop in Average Room Rates due to overbuilding in Sharm el Sheikh and Hurghada. Cairo, despite a decline in occupancy, has been able to raise its average room rate between 1997 and 1998 (See Exhibit 22-9, Average Room Rate % Change). The better measure of hotel performance is RevPar and Mecca has seen the largest increase as pilgrims return to the holy city in large numbers. The Luxor area is still devastated from terrorist attacks and has seen its RevPar drop over 75% in 1998 from 1997 (see Exhibit 22-10).

Exhibit 22-9 Average Room Rate—% Change 1997–1998

Source: HVS International

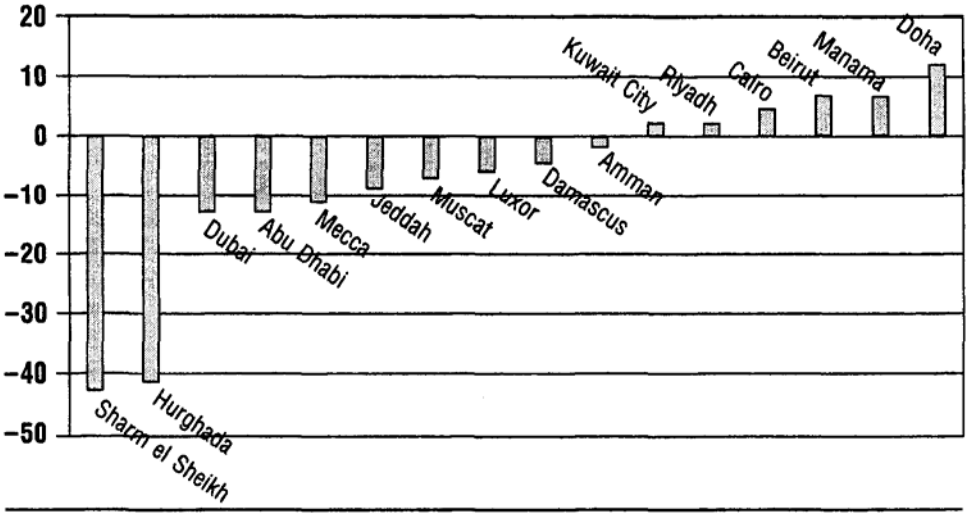
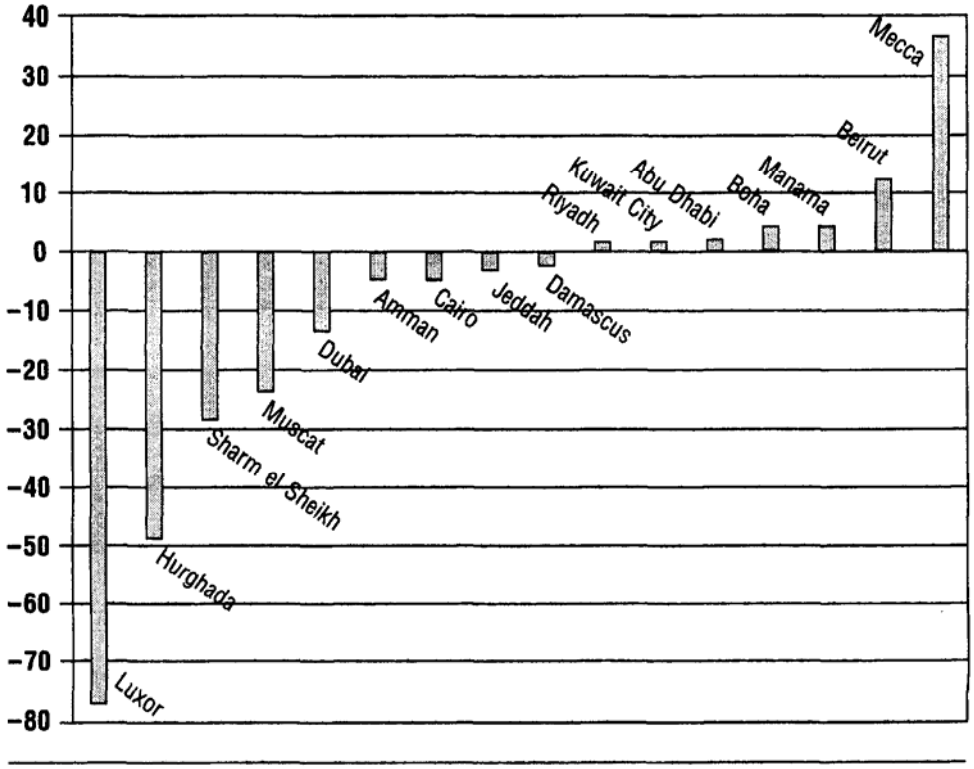


Exhibit 22-10 RevPAR—% Change 1997–1998

Source: HVS International

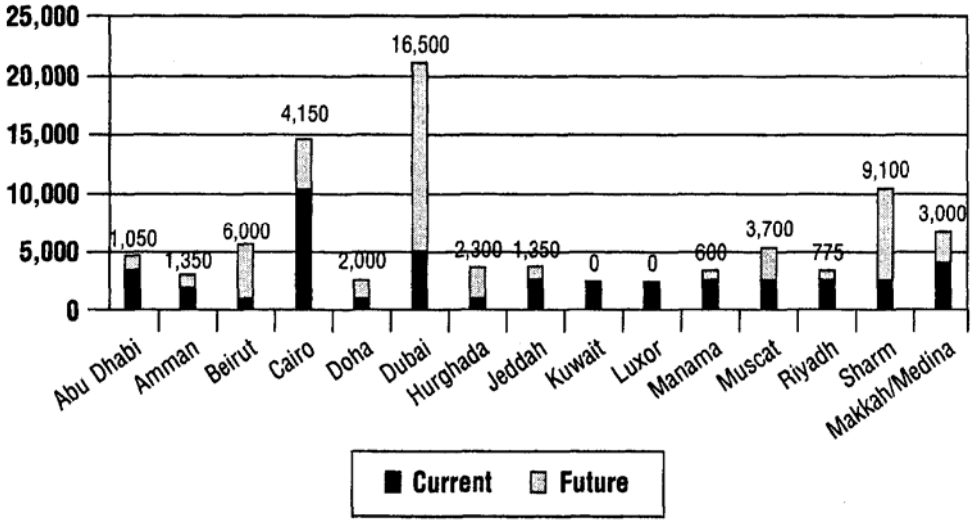


As the area tries to develop its tourist base, a large number of new hotel projects are planned for the future (see Exhibit 22-11, Current and Future Supply). Dubai plans to add over 16,500 rooms in the future in an attempt to become a major tourist destination. It currently has 5,000 rooms and so this would represent a three-fold in-

crease in rooms for an unproven market. Sharm and Makkah/Medina are also planning on an increase in tourist and business travel by planning for 9,100 and 3,000 room increases, respectfully. Beirut, after years of being devastated by civil war is counting on political stability to once again develop its tourism industry that was so important before the civil war by adding over 6,000 rooms in the future. Cairo is also planning to add over 4,000 rooms as it seeks peace with its fundamentalist minority.

Exhibit 22-11 Current and Future Supply

Source: HVS International



» 22.05 COUNTRIES OF THE MIDDLE EAST AND NORTH AFRICA

[1] Bahrain

Tourism continues to be seen as one of the sectors of the economy that will help the island become less dependent on oil revenues. Tourism revenues reached $213 million in 1993, up 20 percent from 1992, while the number of tourist arrivals stabilized at around 1.5 million. Despite the lack of archaeological attractions and the small size of the island, Bahrain was the fifth most popular tourist destination in the Middle East and North Africa in terms of total number of tourists in 1993, capturing 8.4 percent of total arrivals. The popularity of Bahrain is the result of improved road communication with Saudi Arabia via the King Fahad Causeway. Arrivals from Saudi Arabia and other Middle Eastern countries accounted for more than 80 percent of total arrivals in 1993.

Currently, the government's effort to promote tourism-related projects relies essentially on private initiative, rather than public-sector finance. Such projects include the construction of two golf courses and two conference centers as well as the recent completion of the airport extension, which enables the airport to handle up to 10 million passengers per year.

The up-market hotels in Manama City are all operated by international hotel companies, such as Sheraton, Inter-Continental, Hilton International, Forte, Holiday Inn and, more recently, Meridien (1994). Marriott and Oberoi hotels are expected to enter the market in the future.

Commercial business accounts for 65 percent of the up-market room nights in Manama City, while 25 percent is generated by government-related travelers and meeting attendees. The remaining 10 percent consists of individual leisure tourists, primarily from Saudi Arabia.

The government is actively promoting tourism to attract a larger share of tourists from other Middle Eastern countries (particularly Saudi Arabia) as well as Europe and the Far East. Provided that public funding is available to finance the necessary tourist infrastructure, Bahrain should be well positioned to capture more international visitors in the future.

[2] Egypt

Future economic policy will be influenced by Egypt's commitments under the IMF Extended Fund Facility (EFF) accorded in September, 1993. A positive review by the Fund will allow a debt write-off of $4 billion. The government wants to maintain a strong pound in order to prevent capital flight and preserve business confidence. The economic reforms implemented so far should pay off in the form of strong and sustainable growth and declines in consumer prices, which in turn should provide real benefit to Egypt's impoverished population. This should also help to reduce support among the population for the religious fundamentalists. Privatization of state-owned assets is continuing, through limited-share floatations of the 300 or so public enterprises. The government is attempting to tap small investors' savings rather than attract large private investors and thereby maintain control of the public companies while strengthening the sector with private capital.

Despite continuing terrorist activity, Egypt remains one of the leading tourist destinations in the Middle East and North Africa. Egypt captured 2.3 million, or 13 percent, of the total tourist arrivals in the region in 1994; only Morocco and Tunisia attracted more tourists in the same year. The annual compound growth rate of tourist arrivals to Egypt from 1984 to 1994 was 4.2 percent. Preliminary figures for 1995 indicate an increase in the number of tourists by some 21 percent over 1994 figures. Tourism revenue in 1993 was only $1.3 billion (3.6 percent of GDP), down from the record level of $2.7 billion (7.7 percent of GDP) in 1992, Europe (primarily the U.K., Germany, France, and Italy) continues to be the principal feeder market with 48 percent of total arrivals, followed by other Middle Eastern countries with 30 percent of total arrivals. The supply of hotels in Egypt has increased by 8.7 percent between 1989 and 1993, with the development activity concentrated in the new tourist destinations along the Red Sea.

The presence of international hotel companies in the up-market category of the four major markets in Egypt—Cairo, Hurghada, Luxor, and Sharm el Sheikh—is well established. Cairo continues to be one of the main financial and commercial centers in the Middle East and attracts an even mixture of business and leisure travelers. Luxor, with its numerous Pharaonic artifacts, has always been a primary destination for tourists. Egypt's popularity as a winter sun destination is increasing every year.

The most significant factor affecting the economic future of Egypt is the return of international tourism demand, once the threat posed by religious fundamentalists is perceived to have lessened. While prospects for growth in business travel to Egypt are good, the confidence of international investors in the country's economy is closely linked to the future development of tourism. The current development of hotels along the Red Sea is likely to attract a large and previously untapped tourist market to Egypt.

[3] Israel

The majority of tourists to Israel originate from Europe (approximately 60 percent) and North America (25 percent). Beside the negative impact of regional instability, Israel's penetration of source markets around the world has also been limited in the past by Israel's restricted global access and the relatively high cost of travel to and from the country. However, Israel's accessibility has improved significantly in the past two years, following El Al's inauguration of several Far Eastern routes—including Beijing, Bangkok (via Bombay) and Hong Kong—and the Israeli government's implementation of a new "open skies" policy in March 1994, which has brought about a widespread deregulation of the industry. Another important event was the June 1994 agreement between Israel and the Vatican to establish full diplomatic relations. This has resulted in a rapid increase in the number of Christian travelers visiting the numerous religious sites in Israel,

Jerusalem has always been the focal point of tourism in Israel. A recent Ministry of Tourism survey estimates that 91 percent of all tourists who come to Israel visit Jerusalem during the course of their stay. In order to meet the growing commercial and leisure demand, the local municipal and tourism authorities have plans to build an additional 10,000 hotel rooms in the city by the end of the decade.

Tel Aviv is the commercial and industrial heart of Israel. Today, the Tel Aviv "hotel strip" is a row of dated concrete high-rise properties that blight the scenic Mediterranean coastline. However, with several new international hotels in the planning and construction stages, existing hotels are preparing for the new competition. The new 550-room Inter-Continental Hotel, currently under construction and scheduled to open in 1997, represents the first new-build hotel in the city since 1981. Although there are several projects, including a Hyatt, in the planning stages, further additions to supply are likely to be constrained by the lack of available land and spiraling real estate values, which favor non-hotel development.

Eilat has been the site of most of the new hotel construction in Israel in recent years. Today, the resort has more than 5,500 hotel rooms, with a further 5,000 to 6,000 in the planning or construction stage. Eilat's real strengths as a resort are its short-haul proximity (a four- to five-hour flight) from the main tourism-generating countries in Europe and its guaranteed year-round sunshine.

Despite impressive growth in international visitors to Eilat in 1994, market occupancies have been hurt by the opening of several new hotels and an exodus of Israeli vacationers to Turkey, where prices are considerably cheaper. Although Eilat is presently the most developed resort on the Red Sea, it faces stiff competition from the rapidly growing and substantially cheaper Egyptian resorts of Sharm el Sheikh and Hurghada.

The increased interest in Israel as a tourist destination, coupled with the prospect of a lasting peace agreement, could significantly increase the number of leisure, religious, convention, and commercial visitors to the country.

[4] Jordan

The dramatic improvement in Jordanian-Israeli relations has already brought Amman economic dividends in the form of debt relief of approximately $900 million. The mini-boom that Jordan experienced after the Gulf crisis continued in 1994. However, the economy has more recently been constrained by the embargo on Iraq, which is one of Jordan's largest trading partners. The government has announced 121 infrastructure projects aimed at developing the domestic economy and fostering economic cooperation in the region. Special attention has been given to the development of the

Jordan Rift Valley, the creation of a free trade zone in Aqaba and Eilat, and the joint promotion of tourism in the region.

Political instability in the Middle East has historically denied the Jordanian tourism industry the chance to develop to its full potential. Since 1992, however, the number of tourist arrivals has grown rapidly, recording an increase of 15.4 percent in 1993 and 11.6 percent in 1994. Much of this has come from cross-border tourism with Israel. Tourism receipts accounted for $563 million in 1993, representing an 11 percent contribution to GDP. Visitors from Middle Eastern countries dominate the total number of international arrivals. However, when only leisure travelers are considered, tourists from Europe represent the largest market. For the past three years, Italy (28 percent) has been the largest feeder market, followed by the U.K. (17 percent) and Germany (16 percent).

Recently, plans for several hotels in Amman have been announced. Also, the city of Petra has drawn substantial interest from both local investors and international hotel companies and it is expected that, in the next two to three years, between 800 and 1,000 rooms will be added to the existing supply. Several other hotel projects at various planning stages are currently rumored along the Dead Sea and in Aqaba.

[5] Kuwait

Kuwait continues to attract a small number of commercial travelers and almost no leisure tourists. According to the WTO, there were only 73,000 arrivals in 1993. Kuwait has not actively encouraged tourism, although some hotels are attempting to promote weekend/short-break packages targeted at guests from neighboring Middle Eastern countries. In addition, commercial demand has not reached pre-invasion levels because of the continuing threat posed by Iraq. Nearly all visitors (81 percent) to Kuwait are from Middle Eastern countries. Despite the lack of new additions to the current stock of up-market hotels, the Kuwaiti hoteliers do not envisage growth in demand in the short-term.

ADRs in Kuwait City continue to be among the highest in the Middle East and North Africa and reached $175 in 1994 as a direct result of actions taken by the Kuwaiti Hotel Owners Association, which has set a minimum charge for up-market hotels. In 1995, this rate was reduced as the market was forced to become more competitive in order to attract business. However the results of such high average rates can be clearly seen in the occupancy levels. Business and government travelers represent more than 95 percent of total room night demand in the up-market hotels; the remaining 2 percent is generated from individual leisure travelers.

Despite the promotion of short breaks and weekend packages, the tourism segment is not expected to become a major source of demand for hotels in Kuwait City. Hotels are expected to continue to depend largely on government and business travelers for the vast majority of their business. Given the current low occupancy levels, no new up-market hotels are expected to enter the market.

[6] Lebanon

Prior to the civil war, Lebanon was known as the "Switzerland of the Middle East," attracting large volumes of both business and leisure travelers. The country offered a diverse range of tourist attractions, from skiing in the mountains to swimming in the Mediterranean. Today, Beirut remains the capital and the main economic, political, and social center of the country. The stock of hotels in Lebanon has been drastically

reduced in comparison with pre-civil war levels. Today, the entire country has some 4,000 rooms, whereas in the 1970s, Beirut alone had 7,000 rooms.

Currently, there are only a few high-standard hotels operating in Beirut and, because of this, business travelers are forced to pay room rates well in excess of $125 for standard accommodation. These hotels achieve an occupancy of between 50 percent to 60 percent. Improvements in the overall transient accommodation are expected with the addition of new up-market hotel rooms as well as the reconstruction of damaged hotel properties.

Two tourism-related projects are being sponsored by the government: one is a leisure complex including a casino, a theater, and restaurant outlets; the other is a project for a 500-room hotel with a 1,000-seat conference center, likely to be operated by an international hotel company.

[7] Morocco

The tourism industry in Morocco generates more than $1.2 billion, more than 4 percent of the country's GDP in 1993. The major locations of tourism and business interest in Morocco are Rabat, Casablanca, and Marrakech. The capital, Rabat, has only a limited supply of hotels offering international standard accommodation. Casablanca, one of the largest hotel markets in Morocco, is the commercial and financial center of the country. Marrakech is considered to be Morocco's most developed and popular tourist destination; however, its up-market hotels are suffering from a degree of oversupply.

Morocco is expected to remain the leading country in terms of volume of tourists in the region, because of its wide variety of tourist attractions and strong commitment by its government toward the sector. The current privatization program represents a good opportunity for potential investors to gain a foothold in a lucrative market. The long-term challenge for Morocco will be to maintain its unique image and ADR in the face of ever-increasing competition.

[8] Oman

Tourism continues to represent a minimal portion of the national economy, accounting for 1 percent of GNP in 1993. The number of tourist arrivals to the Sultanate was 2 percent of the total number of tourist arrivals to the region in the same year. In contrast with the majority of other Gulf states, however, the largest proportion (approximately 30 percent) of visitors to Oman were from European countries, while arrivals from other Middle Eastern countries averaged only 13 percent per annum. Most of the international arrivals in Oman were business travelers. The government is actively involved in the promotion of the Sultanate's other tourism attractions, such as Nizwa, Rustaq, Mudarib Sur and Salah. It is expected that Oman will continue to attract only a small number of international visitors in the future, both for social reasons as well as the fact that the country's infrastructure is not capable of handling mass tourism at present.

The up-market hotel sector in Muscat has experienced an increase of nearly 10 occupancy points between 1993 and 1994, and a further 2 percentage points in 1995, while ADR has increased $9 in the last two years. The local up-market hotels are expected to see more competition as a result of the addition of the 250-room, five-star Hyatt hotel in 1995. Approximately 60 percent of the room nights in Muscat are generated by corporate and government-related travelers. The remainder is made up of

airline crews (27 percent), leisure travelers (10 percent), and conference attendees (3 percent).

The Sultanate is making an effort to attract more leisure visitors both from other Middle Eastern countries and from Europe. However, the limited tourism infrastructure will prevent Oman from being able to handle large volumes of leisure travelers in the short term. Business travel related to the oil and gas industries is expected to remain the largest market for the local hotel industry.

[9] Palestinian Areas

Because of political and economic problems, demand for hotel accommodation is extremely limited from the commercial sector and nonexistent from the leisure sector. The supply of hotels in the Gaza Strip is limited to small lodging facilities, which account for a total of 92 rooms. Most of the government and commercial travelers are displaced to either Tel Aviv or Jerusalem. The existing hotels are generally outdated and do not provide facilities of an international standard.

It is envisaged that hotel demand in the Palestinian Areas will be dependent almost entirely on the redevelopment efforts in the area, at least in the short term. In fact, the numerous infrastructure projects planned for the area are expected to generate a considerable flow of travelers to the Gaza Strip and the West Bank. Reported published rates for double rooms in the local hotels range from $50 to $80. Plans are currently in place to start construction on the first international standard four- to five-star hotel in Gaza City. The 275-room hotel will be located approximately 2.5 kilometers from the city center and will be managed by Marriott Hotels.

[10] Qatar

In the past, the development of the tourism sector has not been a priority for the Qatari government, and, as a result, there is little official information on the contribution of tourism to the national income.

In 1993, an estimated 160,000 tourists arrived in Qatar, an increase of more than 13 percent compared to 1992. In 1994 it is estimated that 172,000 tourists visited Qatar. This represents less than 1 percent of the total number of international travelers visiting the Middle East and North Africa as a whole. Although the Qatari government has recently started attending international travel shows to attract tour operators to the country, future growth will revolve around business travelers, particularly those involved in the oil and gas industries.

The up-market hotels in Doha registered an occupancy of 75 percent in 1995, up from 61 percent in 1994, while the ADR increased by $3. The Doha area has had an increase in business travelers since the Gulf War, largely because of increased activities in the oil and gas industries. Approximately 70 percent of room nights in the up-market hotels were bought by business and government-related travelers, 20 percent by airline crews, and 10 percent by leisure visitors and conference attendees.

Although Qatar has not actively tried to attract leisure travelers in the past, it has recently started, albeit in a limited way, to encourage international tourists to some of its beach resorts. Sporting events are also expected to generate leisure tourism, specifically from Middle Eastern countries and other Arab states.

[11] Saudi Arabia

International tourism continues to be limited in Saudi Arabia, with strict visa requirements making it virtually impossible to visit the country for leisure purposes. There are very limited tourist statistics available, and only recently has some official data been published. However, the kingdom does attract a massive annual pilgrimage, being the keeper of the Islamic holy sites Mecca and Medina. In 1993, there were an estimated two million international arrivals, of which the majority were Muslim visitors to the holy sites.

Principal destinations remain the capital city, Riyadh, the commercial city, Jed-dah, and the holy cities of Mecca and Medina. Jeddah is the financial and commercial center as well as the main leisure destination. Seven hotels currently under construction will be operated by international hotel chains.

Non-pilgrimage tourist demand in Saudi Arabia will continue to be dominated by business travelers. Saudi Arabia will also follow the Middle Eastern trend of attracting more intra-regional travelers.

[12] Syria

The tourism industry offers a small contribution to GDP, accounting for an estimated 2 percent of the national wealth and only 4.1 percent of total international tourist arrivals to the Middle East and North Africa in 1993. This limited contribution can be partly attributed to the government's lack of international tourism promotion. The country's political stance has also been a strong deterrent to investments in tourism, despite the abundance of unexploited archaeological and historical sites in the country. The poor tourist-related infrastructure, the limited supply of Western-standard hotels, and the country's historic isolation from the West have disinclined international tourists from visiting Syria.

Damascus remains the focus of any future growth in tourism. Over 70 percent of the estimated 700,000 visitors to Syria arrive from other Middle Eastern countries, while Europe, the second largest geographic market, represents only 15 percent of total tourists.

The supply of up-market hotels in Damascus is very small in comparison with other capital cities in the region. Despite the drop in occupancy rates from 1993 to 1994, occupancy totals in Damascus are still among the highest in the region, primarily because of limited competition.

Syria has tremendous potential for tourism development, having a diverse geography of deserts, mountains, and seashores rich in historical significance, and there is an increased level of interest among major international hotel chains in Damascus. However, a significant influx of international tourists will not occur until Syria is perceived to be a more open and inviting destination.

[13] Tunisia

Tourism is a growing sector of the economy, accounting for more than 7 percent of total GDP in 1993, despite Tunisia's proximity to troubled Algeria and isolated Libya. The tourism industry in Tunisia is concentrated on less than 100 kilometers of the country's 1,300 kilometers of coastline, with the major share of investment concentrated in the resort areas of Hammamet/Nabuel, Sousse/Monastir, and the island of Jerba. Germany is by far the largest feeder market, followed by France, the U.K. and Italy. Europe accounted for 55 percent and Africa 23 percent of total tourist arrivals

in 1993. The continuing popularity of Tunisia as a tourism destination has spurred considerable investment in new hotel development, primarily along the coast.

Tunis and Hammamet are the major locations of tourism and business interest in Tunisia. Tunis has a limited supply of hotel rooms, dominated by Hilton, Meridien, and the domestic chain, Abou Nawas. Despite being the largest resort in Tunisia, Hammamet has only one property operated by an international hotel company, Sheraton.

The low occupancy levels achieved by hotels in Tunis and Hammamet in 1990 and 1991 were a direct result of the Gulf War. The business segment is the largest demand segment in Tunis (85 percent), with the balance made up by leisure groups and airline crews. In contrast, Hammamet hotels derive 85 percent of their demand from the tour operator market, and the balance from individual leisure travelers and incentive/conference business. ADR in Tunis hotels has stabilized at close to $60 since 1992. However, in Hammamet, a price war among local hotels and an increased supply of hotels has meant that ADRs have constantly dropped since 1992.

[14] United Arab Emirates

The United Arab Emirates (UAE) has experienced a greater amount of tourism development during the past three years than any other nation in the Arabian Peninsula. Although Abu Dhabi is both the wealthiest emirate and the capital of the UAE, Dubai has the larger tourism market, with three golf courses, a race track, and a marina. Arrivals to Dubai now account for more than 6 percent of total tourists in the Middle East and North Africa. Although visitors from Middle East countries still represent the majority of visitors to Dubai (37 percent including UAE nationals), the share of Europeans increased from 20 percent in 1992 to 27 percent in 1993. An estimated 71,000 tourists from the former Soviet Union visited Dubai in 1993 and, although considered tourists, many of them visited the emirate to take advantage of Dubai's low consumer prices.

The uplift in occupancy in up-market hotels in Abu Dhabi was moderated by recent supply increases. Despite an increase in room supply, Dubai hotels achieved one of the highest occupancies in the Middle East and North Africa in 1994, with 74 percent, up from just 70 percent in 1993. It is expected, however, that occupancy will remain relatively flat or decline slightly in both Dubai and Abu Dhabi during the next few years to absorb the new supply. In addition, increased competition will be generated by small residence hotels (sixty to eighty rooms) catering to extended-stay guests who normally stay in up-market full service hotels.

While the UAE will capture more visitors in the future, Dubai will continue to be the dominant market, attracting both business travelers and an increasing number of leisure tourists traveling on package holidays. Given the significant level of recent hotel construction, as well as the development of more hotels in both Dubai and Abu Dhabi, it remains to be seen whether demand will be able to keep up with supply.

[15] Yemen

The tourism contribution to the national economy in Yemen accounts for less than 0.3 percent of GDP. The number of visitor arrivals has remained stable between 1992 and 1993 and dropped in 1994 as a result of a civil war. European nationals are by far the largest portion of visitor arrivals, accounting for 64 percent of the total. With the government's recent focus on oil exploration, the vast majority of European travelers in Yemen are business travelers to Sana'a or Aden. The lack of tourism infrastructure and the unstable political environment means that significant volumes of leisure trav-

elers are unlikely to visit the country in the near future. The presence of international hotel chains is very limited, with only Sheraton, Taj, and Movenpick currently represented. Holiday Inn will soon manage a 200-room hotel in Aden.

The lack of leisure tourist infrastructure, combined with the unstable political environment, will prevent Yemen from attracting many leisure tourists in the foreseeable future. Any growth in the number of visitors will continue to be generated primarily from commercial business travelers seeking opportunities in the country's growing oil and gas explorations.

» 22.06 ASIAN MARKETS VALUES

[1] Hotel Values 1993 to 1997

In general, the strong growth of the economies in Asia, prior to 1997, had a positive impact on the performance of hotels throughout the region. In many instances, occupancy levels continued to grow as demand outpaced new supply. At the same time, hotels are able to increase their rates, overall profitability and, subsequently, their asset values. This upward trend in most markets is clearly demonstrated by the increases in hotel values from 1993 to 1996 (see Exhibit 22-12 and Exhibit 22-13).

Exhibit 22-12 Asian HVI In US$ Ranked by Index in 1997

Source: *HVS International*

	1993	1994	1995	1996	1997
Hong Kong	1.620	1.989	2.616	2.861	2.221
Tokyo	2.769	2.484	2.603	2.300	1.984
Average	1.000	1.114	1.265	1.298	1.158
Singapore	1.113	1,298	1.626	1.463	1.134
Seoul	0.912	1.230	2.009	1.492	1.119
Mumbai	0.872	1.077	1.484	1.319	1.004
Shanghai	0.667	0.884	1.215	1.096	0.947
Beijing	0.599	0.816	1.142	0,973	0.789
Jakarta	0.912	0,880	1.009	0.973	0.778
Manila	0.482	0.530	0.644	0.890	0.778
Ball	0.434	0.539	0.612	0.655	0.599
Bangkok	.0792	0.892	1.174	0.960	0.578
Kuala Lumpur	0.828	0.743	1.119	0.989	0.477

Between 1993 and 1996, values throughout the region increased by 30% on average. Manila recorded the strongest increase at 80%, closely followed by Hong Kong at 72%. During the period, the only city to show a value decline was Tokyo (at minus 19%), reflecting Japan's prolonged recession.

In the middle of 1997, this strong performance was interrupted by the onset of turmoil in the Asian economies. Sharply declining occupancy levels and room rates caused hotel values to decline by 11% on average in 1997, Kuala Lumpur experienced the most significant drop of almost 45%, followed by Bangkok at 31%. With

the exception of Bali and Manila, all other markets saw a decrease in hotel values during 1997.

By the end of 1997, only hotel values in Hong Kong, Tokyo, Singapore, and Seoul continued to remain above the Asian Average of around US$288,250 per room. This figure is only slightly above the Asian-wide average of US$277,0000 achieved in 1994, and is significantly below the Asian-wide average of US$314,000 achieved in 1995, indicating the severe impact of the economic turmoil on hotel values in Asia in 1997.

Exhibit 22-13 Hotel Values per Room in US$ Ranked by Value in 1997

Source: *HVS International*

	1993	1994	% Change	1995	% Change	1996	% Change	1997	% Change
Hong Kong	403,000	495,000	22.8%	573,000	15.8%	694,000	21.1%	619,000	-10.8%
Tokyo	689,000	618,000	-10.3	570,000	-7.8	558,000	-2.1	553,000	-0.9
Singapore	277,000	323,000	16.6	356,000	10.2	355,000	-0,3	316,000	-11.0
Seoul	227,000	306,000	34.8	440,000	43.8	362,000	-17.7	312,000	-13.8
Mumbai	217,000	268,000	23.5	325,000	21.3	320,000	-1.5	280,000	-12.5
Shanghai	166,000	220,000	32.5	266,000	20.9	266,000	0.0	264,000	-0.8
Beijing	149,000	203,000	36.2	250,000	23.2	236,000	-5.6	220,000	-6.8
Jakarta	227,000	219,000	-3.5	221,000	0.9	236,000	6.8	217,000	-8.1
Manila	120,000	132,000	10.0	141,000	6.8	216,000	53.2	217,000	0.5
Bali	108,000	134,000	24.1	134,000	0.0	159,000	18.7	167,000	5.0
Bangkok	197,000	222,000	12,7	257,000	15.8	233,000	-9.3	161,000	-30.9
Kuala Lumpur	206,000	185,000	-10.2	245,000	32.4	240,000	-2.0	133,000	-44.6

[2] Hotel Values 1998

More recent statistics show a further and more dramatic decrease in hotel values throughout the region during the first half of 1998. On average, values have declined by approximately 20%. All markets—with the exception of Seoul, Shanghai, Singapore, Manila, Mumbai, and Tokyo—have shown a decline in excess of 20 percent, with Hong Kong and Jakarta experiencing a decrease of greater than 40%. Bangkok is the only market in which hotel values have increased in 1998 (see Exhibit 22-14).

On average, hotel values have declined by approximately 27% since their peak (see Exhibit 22-15). Interestingly, in most markets, values peaked at the end of 1995 and started to decline before the economic crisis, primarily as a consequence of rising supply. The markets that have witnessed the greatest value declines are Kuala Lumpur (58%), Jakarta (48%), and Hong Kong (47%). Manila has only seen a decline of 7%.

While values have shown dramatic declines, to-date there is little or no evidence of sales occurring at these levels. Even prior to the economic crisis, very few significant sales of hotels occurred. Most activity was focused on new developments rather than the acquisition of existing properties. Partly as a consequence of ineffective bankruptcy laws, as well as the long-term view taken by most Asian investors, so far very few hotels have been offered for sale at realistic current values. HVS' analysis has shown that Asian hotels are currently trading at historically low values, but there are few true opportunities to actually capitalize on these depressed levels.

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Exhibit 22-14 Value per Room Comparison in US$ (December 1997 and July 1998)

Source: HVS International

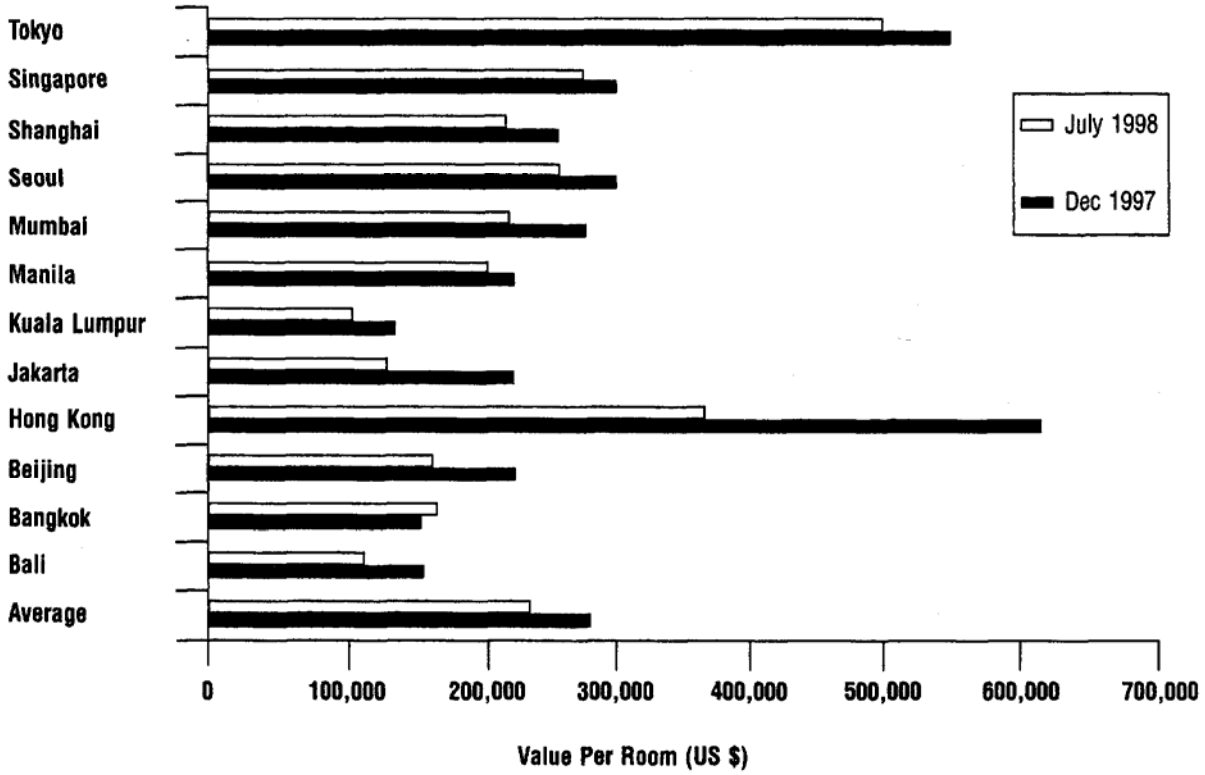
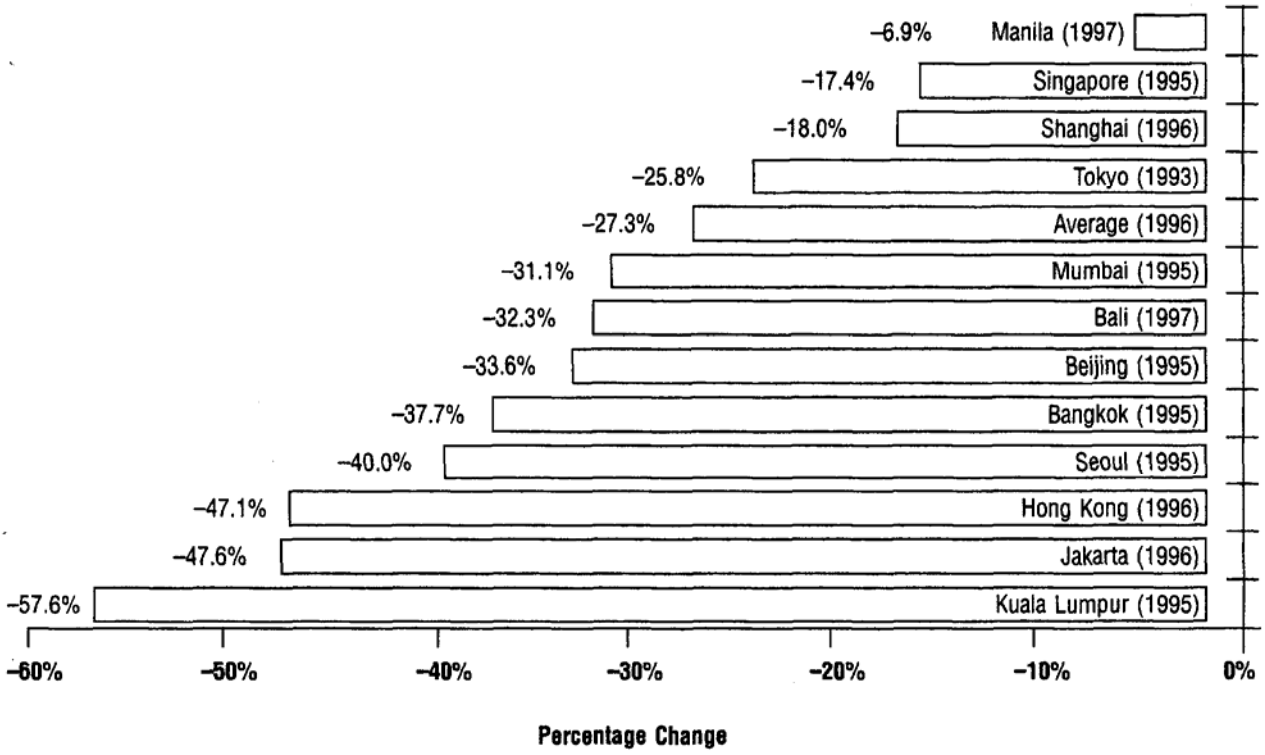


Exhibit 22-15 Percentage Change from Peak Value

Source: HVS International



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» 22.07 THE ASIAN COUNTRIES

[1] JAKARTA AND BALI, INDONESIA

Although occupancies increased annually in Jakarta during the period 1993 to 1996, increased competition as a result of new supply limited increased in room rates, keeping room yields relatively stable. By the end of 1997, the economic crisis and the devaluation of the rupiah caused domestic social unrest and political riots in Jakarta and other parts of Indonesia, severely affecting both national and international demand. Hotel values dropped in 1997 after peaking in 1996.

As supply has remained relatively stable during the last four years, hotels in Bali have benefited from rising occupancy levels and average room rates. The combination of new supply and travelers' growing negative perceptions of Indonesia resulted in a drop in room yields during the first part of 1998.

After the stepping down of the former President Suharto in early 1998, the country accepted the IMF package to rescue the national banking system and economy. Among other plans, the government has introduced new legislation empowering banks to foreclosure more easily on defaulting borrowers, allowing transactions to take place more quickly than before.

Although the immediate economic outlook for Indonesia is improving in-line with the implementation of new laws and strengthening of the rupiah, hotel room yields are expected to increase only marginally, as new supply in both markets is likely to dilute any future demand growth. Hotel values are not expected to increase within the next 12 months.

[2] Hong Kong

Strong demand growth and significant annual occupancy and average room rate growth during 1994 to 1996. As a result, profitability increased and asset values peaked in 1996. The strong dependence of Hong Kong on travelers from other Asian countries was felt strongly as soon as the currencies of feeder markets were devalued during 1997, when hotel occupancies dropped by almost 10% and average room rates declined significantly.

Although occupancy levels have started to recover, average room rates are still far below the 1996 levels, making it unlikely that Hong Kong will see pre-crisis hotel values for some time.

[3] Beijing and Shanghai, PR of China

Although hotel values in Beijing and Shanghai peaked in 1996, average room rates and occupancy levels remained relatively stable during the period form 1995 to 1997. New supply only marginally affected occupancy and average room rate levels in both cities.

More recent statistics for both markets show a further decline in room yields, causing values to drop during the first part of 1998. The envisaged opening of new hotels, in combination with the persistent economic crisis in Asia, is expected to have a further negative effect on hotel values which are unlikely to reach 1996 levels within the foreseeable future.

[4] Kuala Lumpur, Malaysia

A two-month haze caused by the burning of land by Indonesian farmers, combined with new supply, the general economic downturn, and subsequent devaluation of the ringgit caused occupancy and average room rates to decline during the first seven months of 1998. New supply and the current political problems in Malaysia are expected to depress the performance of hotels further and a recovery of hotel values in the immediate future is unlikely.

[5] Mumbai, India

Hotel values in the five-star deluxe segment in Mumbai peaked in 1995 and have declined since. Although the average room rate continued to increase in 1996 and thereafter, as higher paying international business travelers replaced some domestic demand, hotel occupancies started to decline in 1996, mainly as a result of the slowdown in the domestic economy. With new supply envisaged to enter the market within the next five years, hotel values are not expected to reach 1995 levels within the immediate future.

[6] Seoul, South Korea

Hotel values in Seoul peaked in 1995 and fell by almost 18% in 1996, due to a substantial decline in occupancies and average room rates. This downturn was caused primarily by the instability of the Korean economy and, to some extent, by the opening of the Ritz Carlton Hotel in 1995. Although no new supply has been added to the market since 1995, domestic economic difficulties and the depreciation of the won caused a further deterioration in the performance of the local hotel market during the latter part of 1997.

Like Indonesia and Thailand, South Korea accepted a bailout program from the IMF in order to restructure the banking system and to improve the domestic economy. As no substantial new supply is envisaged to enter the market within the next 12 months, the performance of the existing hotels is expected to improve as soon as the economy starts to benefit from the IMF aid plan and the won regains strength. We expect hotel values to start to increase over the next 12 months. However, the market is vulnerable to the potential recession considering a number of previous postponed hotel projects.

[7] Tokyo, Japan

Unlike other Asian countries, Japan entered a recession in the early 1990s. Subsequently, hotel values have fluctuated in-line with the decline in room yields and net income. Tokyo hotel values achieved their highest level in the early 1990s and have declined every year since 1993.

As the Japanese economy depends on other Asian economies to a large extent, hotel values are not expected to increase within the foreseeable future. However, any improvement in the Japanese economy is likely to have a positive effect on hotel values as limited supply in envisaged to enter market.

[8] Singapore

A relatively stable supply of Singaporean hotels in the 'very large' (more than 601 rooms) hotel segment allowed occupancy and average room rate levels to increase annually during 1993 to 1996. After hotel values peaked in 1996, the 1997 general economic downturn in Asia and the dependence of Singapore on travelers from other Asian countries resulted in a decline in room yields, causing values to fall for the first time in 1997.

Although significant new supply is expected to enter the Singapore hotel market, this will be limited mainly to smaller or lower grade hotels. Nevertheless, the incidence of business travelers trading down to lower classified hotels is likely to affect the occupancy growth of the very large hotels. However, we expect the average room rate levels to be broadly maintained. Although we expect hotel values to increase slightly over the next 12 months, as more people start to travel to Singapore again, we consider that the increase will be modest.

[9] Manila, Philippines

Although occupancy levels started to fall in 1997 for the first time in several years, average room rates continued to grow as manila benefited from strong commercial demand and no new supply; hence, hotel values in greater Manila peaked in 1997

New room supply, further depreciation of the peso, together with the overall economic crisis in Asia are all expected to depress the performance of hotels in Manila further. Although we expect demand for hotel accommodation to increase, new supply is likely to dilute this demand growth. Therefore, we expect hotel values to fall slightly or to stabilize at current levels during the next 12 months.

[10] Bangkok, Thailand

Up until early 1996, little new supply allowed occupancy levels, average room rates and, subsequently, hotel values to increase year-on-year. Although average room rate levels continued to grow, the market-wide occupancy started to fall in 1996, mainly as a result of new supply, causing hotel values to drop for the first time during the 1990s.

The collapse of the Thai economy and the subsequent devaluation of the baht, together with the general downfall of Asian economies, cause occupancies and average room rates to decrease in Bangkok during the latter part of 1997 and early 1998. More recent statistics, however, show a marginal increase in visitation, hence occupancies and average room rates have increased slightly during the last few months. As only limited new supply is envisaged, and a further sterilization of the Thai economy and strengthening of the baht as a result of the IMF rescue package is anticipated, we expect hotel values to continue to increase within the next 12 months.

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CHAPTER 23

Analysis of Casino Gaming

¶ 23.01 Overview of Gambling 23-2
[1] Gross Wagering and Revenue Trends 23-3
[2] Table Game and Device Analysis by Market. 23-3
EXHIBIT 23-1 2004 Adult Population and Potential Gamer Visits Summary 23-4
EXHIBIT 23-2 Gaming Revenue Statistics Summary 23-6
EXHIBIT 23-3 Table Game and Device Analysis by Market 23-7
[3] Publicly Traded Gaming Corporations 23-8
[4] Consumer Profile and Feeder Markets 23-8
EXHIBIT 23-4 Publicly Traded Gaming Corporations and Suppliers 23-9
EXHIBIT 23-5 Demographic Portrait of Casino Players, 1998 23-10
EXHIBIT 23-6 Casino Spending vs. Other Forms of Discretionary Spending 23-11
[5] The Future of Gaming 23-11
¶ 23.02 Riverboat Gaming 23-11
[1] Illinois 23-12
[2] Mississippi 23-12
[3] Iowa 23-12
[4] Louisiana 23-13
[5] Missouri 23-13
[6] Indiana 23-13
[7] Expansion 23-14
¶ 23.03 Native American Gaming 23-14
[1] The Indian Gaming Regulatory Act (IGRA) 23-15
[2] National Indian Gaming Commission (NIGC) 23-17
¶ 23.04 Gaming Supply and Demand Analysis 23-17
[1] Market Segmentation 23-18
[a] Local Demand 23-18
[b] Tour and Travel Demand 23-19
[c] Leisure Demand 23-19
[2] Win per Unit per Day (WPUPD). 23-19
EXHIBIT 23-7 Analysis of Cripple Stream Gaming Market 23-20
EXHIBIT 23-8 Analysis of Supply and Demand Trends 23-21
¶ 23.05 Forecast of Gaming Win 23-22
[1] Step One—Fair Share 23-23
[2] Step Two—Forecasting Marketwide Gaming Revenue . . . 23-23
EXHIBIT 23-9 Projected Marketwide Gaming Inventory and Calculated Fair Share. 23-23
[3] Step Three—Projected Market Penetration Rates. 23-24
EXHIBIT 23-10 Forecast of Marketwide Gaming Revenue—Cripple Stream Market 23-24
EXHIBIT 23-11 Projected Penetration Rates and Captured Gaming Revenue 23-25
[4] Step Four—Projecting WPUPD. . . 23-25
EXHIBIT 23-12 Projected WPUPD and Total Gaming Win 23-25
¶ 23.06 Distance-Based Vistation Model—Riverboat Casinos 23-26
[1] Step One—Concentric Circle Analysis. 23-26
EXHIBIT 23-13 Estimated Base Population and Visitation Levels. 23-27
[2] Step Two—Forecasting Adjusted Capturable Population and Visitation 23-27
[3] Step Three—Projecting Casino Visits Within the Market 23-27
EXHIBIT 23-14 Base Population and Visitation Levels, Applied Growth Rates, and Overlap Adjustments 23-28
[4] Step Four—Projecting Casino Admissions 23-28

EXHIBIT 23-15 Calculation of Gaming Incidence Factor and Projected Annual Casino Visits . . . 23-29
EXHIBIT 23-16 Estimated Market Capture and Projected Number of Admissions 23-30
[5] Forecasted Win per Admission . . . 23-30
EXHIBIT 23-17 Forecasted Win per Admission 23-31
EXHIBIT 23-18 Forecasts of Marketwide Gaming Revenue and Subject Property's Gaming Revenue 23-32

» 23.01 OVERVIEW OF GAMBLING

Gambling is a near-universal pastime. The origins of gambling and the objects used in the ritual date back to our paleolithic ancestors who tossed polished dice-shaped bones, called astragalia. It is uncertain whether these objects were cast for prophecy, amusement, or to win the possessions of others; in any case, these acts began a custom that has survived throughout the ages. It was the gamblers of sixteenth -century Europe who provided the impetus for the formation of mathematical probability theory, when Antoine Gombauld posed a dice problem to Parisian mathematician Blaise Pascal. Since that time, hundreds of mathematicians, philosophers, and economists have pondered the laws of probability, statistical analysis, and calculus in an effort to master the games of chance.

Because of the widespread popularity of gaming throughout Europe, it is difficult to attribute the origin of gaming in the United States to one period or location. In addition, it is widely noted that Native Americans were enthusiastic gamblers centuries before the arrival of Europeans. The first casinos were placed in the early taverns of New England, where card games and other gaming activities were a part of everyday life. Gaming continued its immigration to America with the French colonization of New Orleans, and spread rapidly throughout the South, then north up the Mississippi. Following the Civil War, gaming in the form of state lotteries was introduced to replenish and rebuild the devastated South. As such, gaming flourished within the region, and soon the state of Louisiana became the center of all gaming activity in the United States. The gaming movement swept west with the "Gold Rush" (1848-1849); in many Western territories, gaming was declared neither legal nor illegal. As a result, gaming proliferated throughout the West until the early 1900s. Ironically, Nevada passed the first law banning gambling in the West, in 1910.

The modern era of casino gaming, as it is known today, began in 1931, when a bill to legalize gaming in Nevada was passed by the Nevada State Legislature in Carson City. Nevada enjoyed a monopoly on casino gaming until 1976, when New Jersey passed a referendum allowing legalized casino gambling in Atlantic City. Over the years, much suspicion regarding criminal involvement has surrounded the casino gaming industry in both Nevada and New Jersey. However, the tremendous amount of regulation on the part of both the Nevada and New Jersey gaming commissions has effectively eliminated the criminal element from the daily operation and ownership of legalized casinos. Although it is reported that elements of organized crime occasionally infiltrate a casino operation, these instances are relatively rare. Today's gaming industry, with its Wall Street backing, has become an accepted industry throughout the United States.

One form of gambling or another is now available in forty-eight of the fifty states. Casino-style gaming is currently legal in twenty-two states, in a variety of forms such as on riverboats, at riverside docks, and in saloons, and on various sites including Indian reservations, public parcels and waterways, and privately owned land. A combination of consumer acceptance and the local municipalities' need to increase revenue has resulted in an array of new jurisdictions and gaming venues.

[1] Gross Wagering and Revenue Trends

Exhibit 23-1 presents the 2000 Gaming Residence and Future Revenue trends in the U.S. gaming industry. "Handle" is defined as the gross amount wager at any form of gambling, or the total amount of money wagered against the house. "Gaming Revenue" is defined as the total amount of money wagered against the house (handle) less winning payouts, or the total amount of money retained by the house from gaming transactions. From the consumer perspective gross gaming is the price paid for playing a commercial game.

Overall, total gaming revenue increased at an average annual rate of 10.2 percent from 1998 to 37.8 billion dollars.

Exhibit 23-2 shows the increase in gaming revenue by different gaming jurisdictions for the year 2000. Nevada continues to lead the nation with approximately 9.6 billion dollars in gaming revenue. Atlantic City is still in second place with approximately 4.3 billion dollars in gaming revenue. Mississippi gaming revenue continues to grow at a healthy pace and is now the third largest casino market in the country with approximately 2.6 billion dollars in gaming revenue. This represents a growth of 5.3% from the prior year.

Nevada's gaming revenue increased by 11.9% from 1998 and this can be attributed to the opening of the several new mega-resorts in Las Vegas market during the year (Bellagio late 1998, Mandalay Bay, Venetian, and Paris). New Jersey with the lack of any new development has shown the smallest increase in revenue growth of all gaming jurisdictions at 3.4%.

[2] Table Game and Device Analysis by Market

Exhibit 23-3 provides an analysis of gaming win segmented into table game revenues and gaming device revenues. The operation, odds structure, playing habits, and derivation of win for table games and gaming devices are distinct and should be analyzed separately, given the available data. The following table presents total win by market, the total number of units within the market, and the win per unit per day (WPUPD) statistics for 1996 and 1997. The WPUPD figure is calculated by dividing the total gaming win by the number of units and dividing that figure by the total number of days in the period.

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Exhibit 23-1 2005 Adult Population and Potential Gamer Visits

Source: *Bear, Steams & Co. Inc.; PricewaterhouseCoopers.*

Market	2005 Potential Gamer Visits	2000 Gaming Revenue (MM)	2005 Gaming Revenue Potential (MM)
Connecticut			
Ledyard/Montville, CT(1)	27,360,197	$1,868.9	$2,835.3
Illinois			
Chicagoland(2)	24,182,195	$2,015.4	$2,803.3
Peoria	1,973,052	$129.6	$165.2
Metropolis	1,796,816	$108,6	$159.7
Indiana			
Southeastern Indiana	8,345,420	$697.4	$1,026.1
Evansville	1,070,003	$96.6	$108.6
Iowa			
Council Bluffs	9,902,919	$347.3	$442.5
Quad Cities(3)	4,899,763	$210.2	$256.0
Dubuque	2,702,159	$115.9	$134.4
Des Moines	4,070,497	184.9	$233.3
Sioux City	940,216	$35.2	$49.4
Ft. Madison	635,030	$30.0	$30.9
Louisiana			
New Orleans	13,540,633	$516.9	$674.3
Lake Charles	6,764,033	$341.3	$408.6
Baton Rouge	2,903,699	$163.9	$201.5
Shreveport	12,604,306	$685.0	$871.4
Mississippi			
Gulf Coast	12,231,656	$1,117.3	$1,431,7
Tunica	7,866,283	$1,194.3	$1,411.3
Vicksburg	4,793,825	$234.7	$278.1
Greenville	1,823,680	$73.0	$76.8
Natchez	891,824	$36.3	$46.7
Missouri			
Caruthersville	391,495	$22.8	$23.4
St. Louis	16,942,962	$683.8	$996.1
Kansas City	13,494,436	$560.0	$749.8
New Jersey			
Atlantic City	35,700,845	$4,164.2	$5,085.5
Nevada			
Las Vegas(4)	41,036,842	$6,075.0	$7,506.1
North Las Vegas	7,714,864	$236.0	$329.1
Laughlin	5,167,014	$559.7	$650.0
Reno-Sparks	7,693,069	$1,026.7	$1,148.7
South Lake Tahoe	5,018,663	$352.7	$424.5
Michigan/Canada			
Detroit-Windsor	17,408,140	$1,233.2	$1,724.4
Halifax	1,128,892	$36.0	$49.4
Hull	3,657,599	$129.3	$166.9
Montreal	6,214,941	$302.7	$377.1
Niagara Falls	8,376,480	$393.6	$392.0
Orillia	4,700,755	$313.2	$311.8
Point Au Pie	1,211,886	$23.6	$33.4
Sydney	423,209	$18.2	$19,1

(1) Assumes slot win at 70%. (2) Illinois and Indiana properties.

(3) Illinois and Iowa properties

(4)LV gross gaming revenues include Boulder Strip, LV Strip, and Downtown LV.

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Exhibit 23-2 Gaming Market Performance ($ in millions)

Source: Bear, Steams & Co. Inc.; State Gaming Control Boards.

Market	1999	Jan-00	Feb-00	Mar-00	Apr-00	May-00	Jun-00	Jul-00	Aug-00	Sep-00	Oct-00	Nov-00	Dec-00	2000
Colorado	$551.3	$49.6	$51.1	$52.5	$51.3	$51.6	$52.8	$60.0	$55.4	$54.4	$54.4	$49.6	$49.1	$631.9
% *Change*	*15.0%*	*17.3%*	*20.2%*	*17.1%*	*20.0%*	*9.2%*	*16.7%*	*16.8%*	*10.5%*	72.9%	*13.5%*	5.0%	*18.2%*	*14.6%*
Connecticut[1]	$1,750.3	$138.0	$151.9	$162.1	$158.9	$156.6	$150.2	$177.6	$169.1	$162.1	$158.8	$148.0	$135.5	$1,868.9
% *Change*	*9.9%*	*11.0%*	*15.1%*	*16.5%*	*8.1%*	*5.0%*	*7.8%*	3.9%	*0.7%*	*7.8%*	*2.1%*	5.2%	7.3%	6.8%
Delaware	$412.5	$38.5	$37.8	$38.7	$45.9	$37.3	$38.1	$49.3	$38.8	$39.3	$46.1	$36.2	$39.1	$485.1
% *Change*	*17.6%*	*15.6%*	23.3%	*23.1%*	42.9%	-5.3%	*19.8%*	*40.7%*	-77.7%	79.5%	72.7%	9.7%	47.6%	26.0%
Illinois	$1,362.9	$130.0	$137.2	$147.9	$141.1	$139.1	$136.8	$147.0	$141.5	$140.4	$141.4	$134.8	$121.2	$1,658.2
% *Change*	23.7%	47.7%	42.2%	*41.1%*	*31.8%*	37.6%	33.3%	*11.8%*	*10.7%*	*15.4%*	9.6%	8.6%	-2.4%	27.7
Indiana	$1,557.0	$131.1	$144.8	$154.0	$143.1	$140.9	$135.5	$151.3	$142.2	$144.7	$140.4	$138.1	$122.9	$1,689.1
% *Change*	*16.2%*	*20.2%*	*13.9%*	*14.0%*	5.7%	4.4%	*11.0%*	*6.8%*	7.9%	*11.8%*	3.3%	8.7%	-2.5%	8.5%
Iowa	$827.3	$72.5	$76.2	$80.5	$74.0	$69.2	$77.0	$79.4	$76.1	$76.4	$73.6	$68.4	$62.6	$885.9
% *Change*	*8.4%*	*22.5%*	*17.9%*	*14.7%*	7.3%	*-^.3%*	*14.9%*	5.7%	7.2%	70.4%	3.0%	*-0.2%*	-6.4%	6.8%
Louisiana	$1,433.6	$133.7	$144.7	$150.5	$139.4	$140.7	$141.1	$155.3	$138.3	$148.7	$136.6	$132.5	$145.6	$1,707.1
% Change	8.3%	*23.1%*	26.3%	*25.6%*	*18.4%*	*22.0%*	*20.7%*	77.2%	*20.0%*	*32.1%*	6.7%	6.2%	74.9%	79.7%
Michigan	$188.4	$55.2	$54.0	$62.7	$60.2	$60.3	$58.8	$66.3	$61.7	$62.4	$63.2	$69.3	$69.1	$743.2
% *Change*	*na*	*na*	*na*	*na*	*na*	*na*	*na*	*1276%*	75%	*84%*	83%	*105%*	49%	294.4%
Mississippi	$2,516.2	$216.4	$229.4	$248.0	$218.4	$220.5	$219.1	$250.0	$228.3	$215.5	$218.5	$207.7	$177.9	$2,649.6
% *Change*	*15.7%*	*12.3%*	*17.4%*	*11.1%*	0.2%	*5.6%*	*2.5%*	7.4%	4.6%	*4.1%*	6.0%	3.8%	*-4.5%*	5.3%
Missouri	$938.4	$80.8	$83.2	$90.9	$83.5	$81.7	$81.4	$86.5	$80.5	$85.9	$83.1	$80.6	$79.5	$997.5
% Change	*10.0%*	*14.6%*	*11.4%*	*13.0%*	*3.9%*	2.2%	*8.3%*	3.6%	2.5%	70.7%	2.8%	3.9%	7.6%	6.4%
Nevada	$9,020.5	$866.5	$751.6	$836.5	$785.7	$799.1	$747.8	$827.6	$814.4	$788.5	$811.3	$799.9	$794.1	$9,602.9
% Change	*11.9%*	7.3%	*14.0%*	*12.0%*	*14.0%*	5.3%	*8.0%*	*12.8%*	6.7%	-3.8%	2.7%	-3.7%	5.7%	6.5%
New Jersey	$4,164.2	$305.9	$337.8	$361.2	$365.5	$362.8	$377.2	$429.3	$404.4	$379.2	$345.1	$336.7	$295.3	$4,300.3
% *Change*	3.4%	*2.2%*	*11.3%*	*7.9%*	*5.6%*	*-1.6%*	*6.1%*	3.7%	0.7%	9.9%	-3.8%	2.4%	-2.7%	3.3%
Total	**$24,722.7**	**$2,218.2**	**$2,199.7**	**$2,385.3**	**$2,266.9**	**$2,259.7**	**$2,215.9**	**$2,479.7**	**$2,350.6**	**$2,297.4**	**$2,272.4**	**$2,181.8**	**$2,091.1**	**$27,219.7**
% Change	***11.2%***	***14.7%***	***19.5%***	***17.5%***	***13.9%***	***8.7%***	***12.9%***	***11.5%***	***6.5%***	***7.0%***	***4.0%***	***3.3%***	**4.0%**	***10.2%***
Native American	$9,614.7	—	—	—	—	—	—	—	—	—	—	—	—	$10,644.3
% Change	73.3%	—	—	—	—	—	—	—	—	—	—	—	—	*10.7%*
Total	**$34,337.4**													**$37,864.0**

[1] Connecticut revenues assume slot win at 70%.

Exhibit 23-3 Table Game and Device Analysis by Market

Source: International Gaming & Wagering Business, August 1, 1995; HVS Gaming Services

	1993 Win (000)	1994 Win (000)	Percent Change	Number of Units (1993)	Number of Units (1994)	Percent Change	1993 WPUPD [1]	1994 WPUPD [1]	Percent Change
Table Games									
Nevada	$2,145,334	$2,628,192	22.5	5,551	5,248	(5.5)	$1,059	$1,372	29.6
New Jersey	1,086,700	1,125,500	3.6	1,288	1,310	1.7	2,312	2,354	1.8
Colorado	24,453	26,875	9.9	249	253	1.6	269	291	8.2
Deadwood, SD	5,047	4,892	(3.1)	79	74	(6.3)	175	181	3.5
Illinois Riverboats	234,130	334,304	42.8	301	469	55.8	2,131	1,953	(8.4)
Iowa Riverboats	6,567	25,143	282.9	79	131	65.8	228	526	130.9
Louisiana Riverboats	5,860	191,293	3,164.4	59	437	640.7	272	1,199 3	40.7
Mississippi Riverboats	315,934	512,511	62.2	440	961	118.4	1,967	1,461	(25.7)
Missouri Riverboats	N/A	66,412	N/A	N/A	313	N/A	N/A	581	N/A
Total	$3,824,025	$4,848,710	26.8%	8,046	8,883	10.4%	1,302	1,495	14.8%
Gaming Devices									
Nevada	$3,944,042	$4,307,727	9.2 %	147,174	156,837	6.6%	$73	$75	2.5%
New Jersey	2,214,600	2,297,300	3.7	24,561	27,041	10.1	247	233	(5.8)
Colorado	235,367	298,810	27.0	10,361	11,472	10.7	62	71	14.7
Deadwood, SD	38,294	40,635	6.1	1,977	2,255	14.1	53	49	(7.0)
Illinois Riverboats	371,555	645,247	73.7	4,296	7,523	75.1	237	235	(0.8)
Iowa Riverboats	38,659	79,696	106.2	1,393	1,934	38.8	76	113	48.5
Louisiana Riverboats	10,376	408,764	3,839.5	1,105	8,204	642.4	26	137	430.6
Mississippi Riverboats	473,901	951,805	100.8	6,951	15,612	124.6	187	167	(10.6)
Missouri Riverboats	N/A	43,880	N/A	N/A	1,557	N/A	N/A	77	N/A
Total	7,326,794	9,029,984	23.2	197,818	230,878	16.7	$101	$107	5.61

[1] Win per unit per day

With approximately 50 percent of the total table game units in 1997, Nevada casinos generated a table game win of approximately $2.7 billion. New Jersey casinos generated approximately $1,2 billion in table game win, despite having only 12 percent of total table game inventory. Mississippi riverboat casinos were a distant third with $500 million in table game win in 1997. In terms of WPUPD, New Jersey's casinos are the most efficient, generating on average $2,176 per table per day. Illinois casinos also posted favorable WPUPD figures of $1,735 per table per day in 1997. The Atlantic City and Illinois markets are similar in their proximity to large population bases and the limited number of casino facilities, which results in high WPUPD figures. Overall, total table game win rose by 5.7 percent in 1997, while the total number of units increased by 5 percent, resulting in a small .23 percent increase in WPUPD.

Aggregate gaming device win increased by 9.2 percent in 1997, led by the secondary markets of Indiana, Missouri, and Iowa, which posted gains of 161.595 percent, 46.94 percent, and 16.01 percent, respectively. During the same period, Indiana, Missouri, and Iowa experienced increases in inventory of 63.9 percent, 77.33 percent and 16.01 percent, respectively. The result was a decrease in WPUPD for Missouri, indicating flat demand at the given level of supply. WPUPD among Indiana and Iowa riverboats rose by 59.61 percent and 12.23 in 1997. The established markets of Nevada and New Jersey increased gaming device inventory in 1994 by 0 percent and 3.75 percent, respectively. New Jersey casinos experienced a slight decrease in WPUPD, indicating a stabilization of demand. Similar to table game WPUPD figures, gaming device WPUPD is strongest in the markets proximate to large population bases with limited inventory. In 1997, New Jersey attained a gaming device WPUPD figure of $221, while Illinois generated a WPUPD of $260. Las Vegas, considered to be a mature, stable market, attained a WPUPD figure of $76, with an inventory of 177,020 gaming devices, or 56 percent of the total gaming devices in the United States. It is this critical mass that separates the Las Vegas market from other gaming jurisdictions, and makes the Las Vegas gaming environment the most competitive in the world.

[3] Publicly Traded Gaming Corporations

Exhibit 23-4 presents a list of publicly traded gaming corporations and suppliers. The chart divides the gaming companies into large cap and small-cap gaming stocks. The most obvious observation is the consolidation, which has taken place in the casino industry in the past few years.

It appears the industry is heading for more consolidation through mergers and acquisitions by the larger casino corporations. The small-cap gaming stocks appear to be the most likely take over targets in the near future.

As can be seen from Exhibit 23-4, gaming stocks had a good year in 2000 with the exception of gaming equipment stocks, which had a terrific year in a down market.

[4] Consumer Profile and Feeder Markets

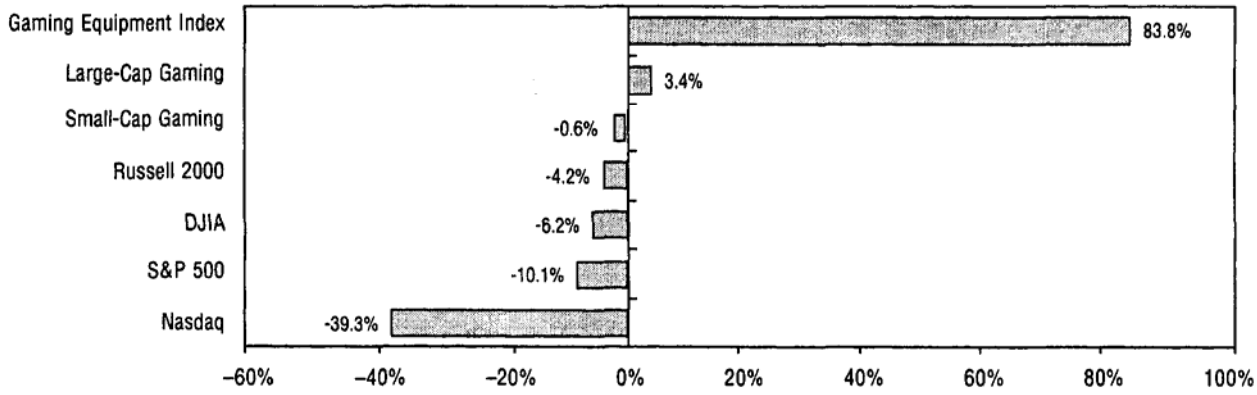
Spending on commercial casino gaming was slightly less than spending on basic cable TV and slightly more than spending on coffee or home video rental and sales.

HVS

Exhibit 23-4 Publicly Traded Gaming Corporations and Suppliers

Source: Bear, Stearns & Co. Inc.; FactSet Research Systems Inc.

2000 Stock Indices Price Performance



2000 and YTD Gaming Stock Price Performance

			YTD Price Perf.		2000 Price Perf.	
Company	**Ticker**	**52-Week High-Low**	**7/12/01 Price**	**YTD % Chg.**	**12/29/00 Price**	**% Chg.**
Large-Cap Gaming Stocks						
MGM Grand §	MGG	$39-$23	$30.55	8.4%	$28.19	12.0%
Harrah's Entertainment	HET	$38-$21	$30.02	13.8%	$26.38	-0.2%
Station Casinos	STN	$19-$12	$15.01	0.5%	$14.94	-0.1%
Park Place Entertainment §	PPE	$15-$9	$11.20	-6.2%	$11.94	4.5%
Mandalay Resort Group	MBG	$28-$18	$25.81	17.7%	$21.94	9.0%
BSC Large-Cap Gaming Index % Chg.				7.4%		*3.4%*
Small-Cap Gaming Stocks						
Ameristar §	ASCA	$19-$4	$17.25	236.6%	$5.13	34.4%
Argosy Gaming §	AGY	$29-$13	$25.86	34.8%	$19.19	23.3%
Aztar Corp.	AZR	$17-$9	$13.35	3.2%	$12.94	19.0%
Churchill Downs	CHDN	$36-$22	$26.70	-10.4%	$29.81	32.1%
Isle of Capri	ISLE	$17-$6	$9.70	-8.7%	$10.63	-19.4%
Boyd Gaming Corp.	BYD	$6-$3	$5.98	74.0%	$3.44	-40.9%
Hollywood Casinos § ^	HWD	$12-$6	$6.50	-29.7%	$9.25	114.5%
Sun International §	SIH	$29-$18	$26.76	12.7%	$23.75	22.6%
Penn National Gaming	PENN	$26-$8	$21.70	113.0%	$10.19	13.2%
Pinnacle Entertainment §	PNK	$23-$7	$6.95	-48.5%	$13.50	-39.8%
MTR Graming	MNTG	$14-$4	$11.45	141.1%	$4.75	55.1%
Trump Hotel & Casinos	DJT	$3-$2	$2.00	6.7%	$1.88	44.4%
BSC Small-Cap Gaming Index % Chg.				25.3%		-0.6%
Gaming Equipment Stocks						
Intl. Game Technology	IGT	$66-$26	$58.13	21.1%	$48.00	136.3%
WMS Industries	WMS	$33-$13	$26.81	33.2%	$20.13	53.3%
Anchor Gaming	SLOT	$67-$23	$55.75	42.9%	$39.00	79.6%
Alliance Gaming	ALLY	$41-$2	$32.76	271.7%	$8.81	224.1%
GTECH Holdings	GTK	$39-$15	$35.76	73.9%	$20.56	-6.5%
Shuffle Master	SHFL	$23-$5	$18.25	72.4%	$10.58	180.1%
BSC Gaming Equipment Index % Chg.				26.8%		83.8%

Exhibit 23-5 shows the demographic portrait of casino players for 1998. The average casino customer has a median household income of $46,000 v. the U.S. median income of $39,000. Also, the average casino customer is better educated than the general U.S. population. Finally, the average casino customer is more likely to be a white collar worker.

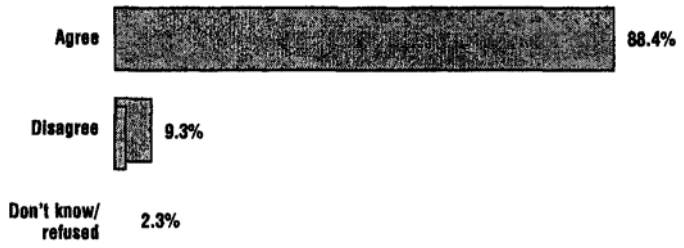
Exhibit 23-6 shows that casino customers spent 22.2 billion dollars in casinos in 1999. The chart compares casino spending to other for forms of discretionary spending patterns. As is clearly shown, Americans spend 358 billion on restaurant meals, making eating out the most popular discretionary spending item among U.S. households.

Exhibit 23-5 Demographic Portrait of Casino Players, 1999

Source: Hart/Luntz

Going to Casinos for Fun

"I primarily go to casinos for the fun and excitement."



Nearly 89 percent of casino customers primarily go to casinos for the fun and excitement.

U.S. CASINO PLAYERS VS U.S. POPULATION, 1999

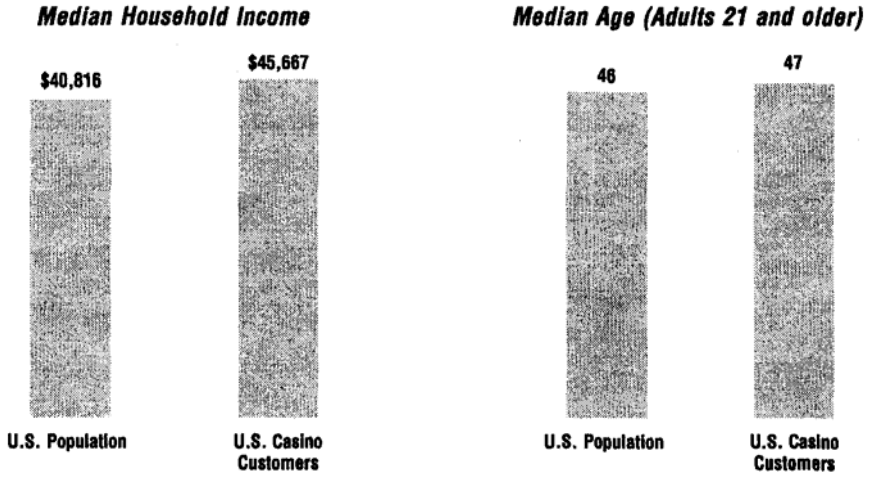
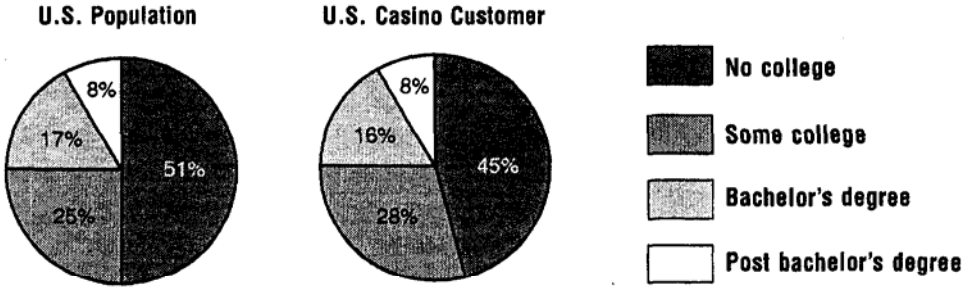


Exhibit 23-5 Demographic Portrait of Casino Players, 1999 (*Cont'd.*)

EDUCATION



Employment

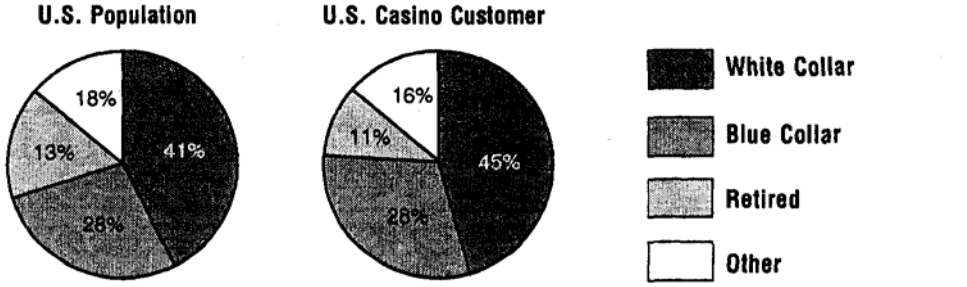
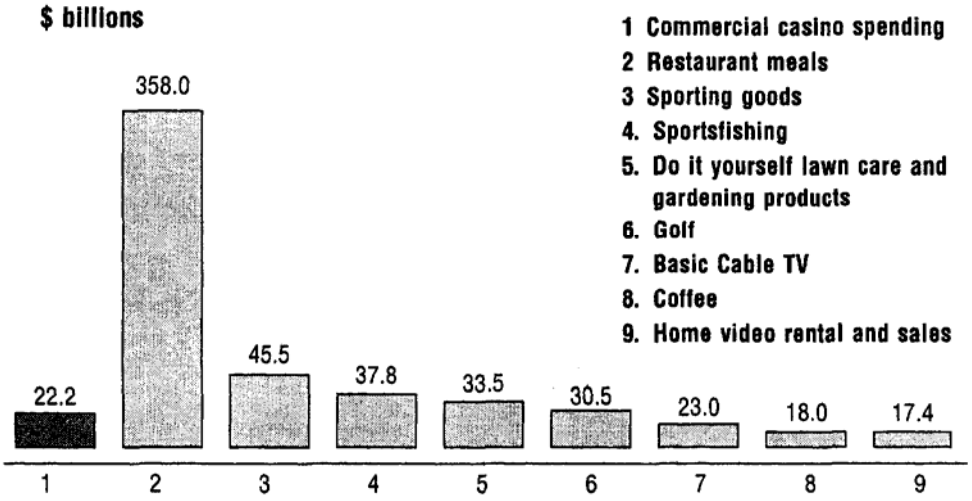


Exhibit 23-6 Casino Spending vs. Other Forms of Discretionary Spending

Sources: 1-Christiansen Capital Advisors, 1999; 2-National Restaurant Association, 1999; 3-Sporting Goods Manufacturers Association, 1999; 4-American Sportfishing Association, 1996; 5-National Gardening Association, 1999; 6-National Golf Foundation, 1998; 7-National Cable Television Association, 1999; 8-National Coffee Association of the USA, 1999; 9-Video Software Dealers Association, 1999



Casino gaming continues to be among the many mainstream spending choices made by Americans. In 1999, consumers spend less on casino gaming than they did on cable TV, golf, and lawn and garden products, but more than on coffee and video rentals and sales.

[5] The Future of Gaming

The gaming industry has seen a dramatic slowdown in the expansion of casino gaming. With the exception of Michigan approving three casinos for the city of Detroit, Michigan in 1996, no new markets have been created for casinos. The industry is currently going through a consolidation phase in which the stronger casino operators are buying out the smaller casinos as competition heats up in most markets. Las Vegas has seen a revival with the opening of the Mirage's Bellagio, Circus Circus's Mandalay Bay, and the Venetian. The addition of the Park Place Paris and new Aladdin Casino, total hotel rooms in Las Vegas will top 120,000 rooms. Currently the new properties are attracting new visitors to Las Vegas and the despite the warnings from many analysts, Las Vegas seems to be absorbing the supply of new rooms without sacrificing profit. Nation wide, it appears that market saturation has taken its tow on Mississippi casino industry as more and more smaller casinos are closing because of the increase in building of new and bigger casinos by the major casino companies such as Mirage, Harrah's, Imperial Palace, and Horseshoe, to name a few.

» 23.02 RIVERBOAT GAMING

The modern era of riverboat gaming in the United States began in April of 1991 with the maiden voyage of the President Riverboat Casino located in Davenport, Iowa. Since that first excursion, riverboat gaming has grown to a more than $3.5 billion industry. Currently, the following six states allow riverboat gaming: Iowa, Illinois, Mississippi, Missouri, Louisiana, and Indiana. The following is a state-by-state overview of riverboat gaming operations.

[1] Illinois

Riverboat gaming in Illinois was legalized in February 1990, and the first boat became operational in September 1991. Currently, a total of ten gaming licenses are allowed, with nine casinos operating as of December 1997. Recent changes in the law now permit Illinois riverboats to remain dockside and do away with the requirement of cruising. This move is intended to allow the Illinois riverboats to be more competitive with Indiana Riverboats which do not cruise in the Chicago area. Illinois riverboats can offer twenty-one, craps, roulette, baccarat, big six, red dog, sic boe, and gaming devices. Adjusted gross receipts, or win, are taxed at a rate of 25 percent, in addition to a $2 per person admissions tax. This is one of the highest tax rates for any gaming jurisdiction.

[2] Mississippi

Riverboat gaming in Mississippi was legalized in April 1990; however, the first boat did not open until August 1992. Mississippi, unlike Illinois, has no restrictions on the number of gaming licenses issued. The number of gaming licenses and the selection of qualified applicants are at the discretion of the Mississippi Gaming Commission. Dockside casinos are permitted on navigable waters in counties adjacent to the Mississippi River or the three southernmost counties adjacent to the Mississippi Sound. Currently, dockside gaming has been approved via a local referendum in nine counties: Adams, Hancock, Claiborne, Issaquena, Warren, Harrison, Washington, Tunica, and Coahoma. Riverboat casinos in Mississippi are not required to cruise and can op-

erate from docks and moorings, resulting in a free flow of pedestrian traffic into and out of the casino twenty-four hours a day. The following table games are permitted within Mississippi riverboat casinos: faro, monte, roulette, keno, fan-tan, twenty-one, seven-and-a-half, big injun, klondike, craps, poker, chuck-a-luck, wheel of fortune, chemin de fer, baccarat, pai gow, beat the banker, panguingui, and gaming devices. Gaming revenues are taxed by the state as well as the counties and local municipalities on a sliding scale. In 1994, the Mississippi Gaming Commission established minimum investment levels for landside developments. All casinos, including those already constructed, must develop a minimum 250-unit hotel equivalent to a Mobil Travel Guide two-star rating and a minimum 500-space parking garage in close proximity to the gaming facility. Alternative developments are allowed at the discretion of the Gaming Commission. Alternative developments must enhance the local entertainment or leisure infrastructure at a cost no less than 25 percent of the cost of the casino. The result of this free market approach to gaming has resulted in a dramatic increase in the number of casinos in Tunica and Gulfport-Biloxi area to become the third largest gaming market in the United States after Las Vegas and Atlantic City.

[3] Iowa

As mentioned, the modern era of riverboat gaming began in Davenport, Iowa, in April 1991, with the opening of the President Riverboat Casino. As of December, 1995, seven riverboats were in operation, located in Bettendorf, Clinton, Davenport, Dubuque, Fort Madison, and Sioux City. The number of gaming licenses issued is at the discretion of the Iowa Racing and Gaming Commission. Currently, the following games are permitted on Iowa riverboat casinos; big six, roulette, poker, craps, twenty-one, red dog, Caribbean stud, 21 super bucks, and gaming devices. Riverboats are required to make a two-hour cruise on at least 100 days between the months of April and October; once the boats meet this requirement, they may operate from their docks. During the docking period, customers may board and disembark the riverboat casino at any time. In May 1994, Iowa reversed several of its restrictive gaming provisions such as the $5 per hand betting limit and the $250 per day loss limit. The market has rebounded, now that the boats are able to compete directly with Illinois boats located just across the Mississippi river.

[4] Louisiana

Riverboat gaming in Louisiana was legalized in June 1991. However, the first boat was not operational until October 1993, because of regulatory and political infighting and disorganization. Currently, fifteen gaming licenses are allowed, with twelve casinos operating as of December 1995. According to the Riverboat Gaming Division, boats must cruise, unless the captain deems the conditions to be hazardous, except in Shreveport, where boats are allowed to operate dockside year-round. Louisiana river-boats can offer twenty-one, craps, roulette, mini-baccarat, big six, poker, and gaming devices.

[5] Missouri

Riverboat gaming in Missouri was legalized in November 1992, with the first boat coming on-line in May 1994. The fate of the Missouri riverboat industry has been much publicized as a result of the ruling by the Missouri Supreme Court outlawing

the use of slot machines on riverboat casinos or elsewhere in the state. The court ruled that games of chance (i.e., slot machines) were unconstitutional and therefore, illegal The situation deteriorated further in April of 1994, when an amendment to the constitution legalizing the games of chance failed to pass by approximately 1,200 votes. However, on November 8, 1994, a referendum to legalize games of chance passed 54 percent to 46 percent. Prior to the referendum, the following games were permitted on Missouri riverboat casinos: poker, craps, twenty-one, Caribbean stud, pai gow poker, Texas hold'em, double down stud poker, and the video representations of these games. Eight riverboats are currently in operation, located in St. Louis, St. Charles, Riverside, Kansas City, and St. Joseph. The number of gaming licenses issued is at the discretion of the Missouri Gaming Commission. Riverboats are required to cruise, unless conditions are such that passenger safety would be jeopardized. Casinos operating along the swift Missouri River in Kansas City have been granted exemptions to allow dockside gaming. However, the casinos must continue to operate "phantom excursions." For continuous dockside operation in other markets, the riverboats must have significant land-based developments resulting in permanent job creation.

[6] Indiana

Indiana's Riverboat Gaming Law was enacted on June 30, 1993. A total of eleven riverboat gaming licenses have been issued within the state of Indiana. Of the eleven licenses, five are in counties bordering Lake Michigan: two in Gary (Lake County), one in Hammond (Lake County), one in East Chicago (Lake County), and one in Michigan City. An additional five licenses were granted to counties located along the Ohio River. Gaming Commission, the following games are permitted: baccarat, twenty-one, poker, craps, slot machines, video games of chance, roulette, klondike, punchboards, faro, keno, numbers tickets, push cards, jar tickets, pull tabs, and big six. The Indiana Riverboats have surpassed all expectations of profitability. In little over three years of operation, the Indiana market does over $1 billion in gross gaming revenue and is still growing. Especially negatively affected by the Indiana river-boats have been the two Illinois casinos in Joliet.

[7] Expansion

As evidenced by the significant amount of revenues generated by riverboat casinos, the industry as a whole has proven to be a successful way for states, counties, and local municipalities to increase revenues without directly taxing their respective residents. However, the socioeconomic impact of riverboat gaming is still being debated throughout the country. While several of the areas supporting riverboat casinos have experienced decreases in unemployment levels leading to economic growth, the social cost and redistribution of discretionary income has yet to be fully measured. Given the flow of discretionary income out of non-gaming states and counties, neighboring legislatures are anticipated to continue seeking approval from voters to bring casinos into their communities. However, the absence of riverboat gaming referen-dums in key states such as Florida, Texas, Kentucky, Ohio, and Pennsylvania reflects the formidable opposition to gaming. From the referendums that were brought to the voters, it is evident that a successful gaming campaign is dependent on well-organized and clearly communicated legislation emphasizing the following issues: regulation, location, distribution of revenues, restrictions, environmental and socioeconomic impact, and law enforcement.

» 23.03 NATIVE AMERICAN GAMING

Since the enactment of the Indian Gaming Regulatory Act (IGRA) on October 17, 1988, Native American gaming activity has increased tremendously throughout the United States. Native American gaming venues can now be found across the nation, from northwestern Washington State to southeastern Florida and from Southern California to eastern Connecticut. Gaming activity taking place on Native American land is classified into three distinct categories as defined in the IGRA:

- *Class I gaming.* This includes social games solely for prizes of minimal value or traditional forms of Indian gaming engaged in by individuals.
- *Class II gaming.* This includes all forms of bingo and other games similar to bingo, such as pull-tabs, and punch boards, provided these are played in the same location as bingo games. Class II also includes certain card games authorized, or not prohibited by state law and played in conformity with statewide regulations and specifically excluding any banking card games, such as baccarat, twenty-one, or any electronic facsimile of such games.
- *Class III gaming.* This includes all forms of gaming that are not Class I or II, including slots, casino games, banking card games, horse and dog racing, pari-mutuel wagering, and jai-alai.

Another concept affecting Native American gaming—and the focus of much controversy—is the gaming compact that must be negotiated between the state and the tribe. The compact is defined as an agreement between sovereigns (tribes and states), similar to a treaty. Tribal/state Class III compacts deal with the sovereign powers (e.g., application of laws and jurisdiction and enforcement of laws) of the parties to the compact. Compacts also delineate the type and quantity of games and/or devices permitted within the casino. Guidelines to establish independent gaming commissions are also included in the compacts. Since the enactment of the IGRA, several court battles have been waged between Native American tribes and state governments over what games are to be permitted in Native American casinos, given the existing state laws on gaming.

[1] The Indian Gaming Regulatory Act (IGRA)

The Indian Gaming Regulatory Act (IGRA) was enacted by Congress on October 17, 1988. According to the IGRA, a principal goal of federal policy is to promote tribal economic development, tribal self-sufficiency, and strong tribal governments. The IGRA was drafted after a congressional committee found that Indian tribes were engaging in gaming activities on Indian lands as a means of generating tribal revenues. Additionally, the study concluded that Indian tribes have the exclusive right to regulate gaming activity on Indian lands if the gaming activity is not specifically prohibited by federal law and is conducted within a state that does not, as a matter of criminal law and public policy, prohibit such gaming activity. It was also concluded that existing federal law did not provide clear standards or regulations for the conduct of gaming on Indian lands.

The purpose of the IGRA is to provide a statutory basis for the operation of gaming by Indian tribes as a means of accomplishing the aforementioned goals. In addition, the IGRA will provide a basis for the regulation of gaming by an Indian tribe to shield it from organized crime and other corrupting influences, to ensure that the tribe is the primary beneficiary of the gaming operation, and to assure that gaming is conducted fairly and honestly by both the operator and players. The IGRA also

established an independent federal regulatory authority for gaming on Indian lands, federal standards for gaming on Indian lands, and the National Indian Gaming Commission. The regulatory authority was deemed necessary to address congressional concerns regarding gaming and to protect such gaming as a means of generating tribal revenue. The IGRA is composed of the following sections;

- Findings
- Declaration of Policy
- Definitions
- National Indian Gaming Commission
- Powers of the Chairman
- Powers of the Commission
- Commission Staffing
- Commission—Access to Information
- Interim Authority to Regulate Gaming
- Tribal Gaming Ordinances
- Management Contracts
- Review of Existing Ordinances and Contracts
- Civil Penalties
- Judicial Review
- Subpoena and Deposition Authority
- Investigative Powers
- Commission Funding
- Authorization of Appropriations
- Gaming on Lands Acquired After Enactment of This Act
- Dissemination of Information
- Severability
- Criminal Penalties
- Conforming Amendment

Of all the sections of the IGRA, the sections dealing with the formation of the National Indian Gaming Commission (NIGC), tribal ordinances, and management contracts have the greatest impact on the feasibility and economic viability of a Native American gaming operation. The formation and purpose of the NIGC is addressed in H 23.03 [2].

The tribal gaming ordinances sets forth a broad overview of Indian gaming requirements and regulations ranging from licensing procedures to background investigations. The following points are outlined within the tribal ordinances section of the IGRA:

- Class I gaming activities are not subject to provisions of the IGRA, while all Class II and Class III gaming operations are.
- An Indian tribe may engage in, or license and regulate, class II and III gaming, as long as the tribe is located within a state that permits such gaming for any purposes by any person or organization.
- With limited exception, the Indian tribe will have the sole proprietary interest and responsibility for the conduct of any gaming activity.

- The net revenues must be used for the purposes of funding tribal government operations and programs; they must provide for the general welfare of the tribe, promote tribal economic development, be donated to charitable organizations, and help fund operations of local government agencies.
- The construction and maintenance of the gaming facility, and the operation of the facility is conducted in a manner that adequately protects the environment and the public health and safety.
- The tribe must have a system for conducting background checks on key managers and employees and must license such officials.
- Tribes may also license an individual or entity to conduct gaming within the limits of applicable state law.

These are the rules for management contracts:

- The permitted fees are up to 30 percent of net revenues with exceptions up to 40 percent.
- The commission must investigate contractors and may disapprove a contract based on such investigation.
- The contract must allow tribal access to daily operations of the game, monthly audits, minimum guaranteed payment to the tribe, and have terms of no more than five years, with exceptions up to seven years.

[2] National Indian Gaming Commission (NIGC)

According to the IGRA, the National Indian Gaming Commission (NIGC) is to be composed of five people, three of whom must be members of federally recognized tribes. The chairman will be appointed by the President of the United States with advice and consent from the senate. The Department of Justice will conduct background investigations of all appointees. Under the IGRA, the NIGC performs a wide variety of regulatory, enforcement, and advisory functions. The follow items illustrate the breadth of NIGC responsibilities in regulating Indian gaming. The NIGC has the authority to:

- Permanently close tribal games;
- Enforce collection of civil fines;
- Enforce tribal gaming ordinances;
- Monitor all Indian gaming activities;
- Inspect gaming premises;
- Conduct background investigations of employees and contractors;
- Access records, books and other documents and audit accounts;
- Conduct any investigation necessary in connection with regulation of class II gaming;
- Consult with law enforcement officials where appropriate; and
- Request the U.S. Attorney General to conduct necessary criminal investigations.

NIGC funding is derived from tribal assessments and congressional appropriations. Assessments are set on a sliding scale from .5 percent to 2.5 percent of the first $1,500,000 of gross revenues and up to 5 percent of amounts in excess of $1,500,000.

» 23.04 GAMING SUPPLY AND DEMAND ANALYSIS

The initial step in analyzing supply and demand trends within a given gaming market is to quantify the existing level of gaming inventory, segmented by table games and gaming devices. To quantify gaming supply levels, a detailed review of all competitive gaming facilities is performed. Once the market's supply level and gaming mix are known, an analysis of the demand for gaming facilities is performed.

Unlike traditional economic models of supply and demand, the price variable associated with gaming is largely determined by the consumer. Gaming is an intangible product: what the consumer is purchasing is the "experience" and "excitement" casino gaming offer. The price that the consumer is willing to pay for this experience is known as the "win," and is quantified on a per-unit basis known as the "win per unit per day" (WPUPD). Research indicates that the WPUPD, or the price a market can bear for gaming activity, is highly correlated with the level of available gaming inventory. The actual WPUPD attained by a market, say $250 per gaming device, provides an indication of the marketwide demand for gaming devices. These demand levels within a market can be estimated through an analysis of the actual WPUPD attained by the market versus the market's theoretical maximum WPUPD. The resultant statistic is known as the market's capacity utilization rate. Historical fluctuations in the marketwide capacity utilization rate at various levels of supply can provide insight into the future demand for gaming. Further affecting the demand for gaming facilities in the market are current and projected trends in economic and demographic factors such as population base, employment, disposable income, and visitation. In addition, seasonal fluctuations must be taken into consideration.

Once the various demand trends have been identified, a variety of analytical methodologies may be employed to forecast gaming revenue for an overall market or an individual property. The employment of a specific methodology must take into consideration the reliability and availability of the data to be utilized.

The following procedures are employed in the analysis of gaming supply and demand trends:

1. Analysis of Supply:
   - Identify all local and regional gaming facilities;
   - Quantify the number of existing and proposed gaming facilities by gaming units (i.e., table games and gaming devices) available in the market area; and
   - Determine whether additional gaming facilities will enter the market in the foreseeable future.
2. Analysis of Demand:
   - Review the area and neighborhood economic and demographic data to determine the market's overall health and ability to support existing and proposed levels of gaming supply;
   - Examine the local and regional demand sources by market segment to determine potential market mix, demand levels, player gaming habits, and the populace's propensity to gamble; and
   - Review historical marketwide trends in WPUPD and capacity utilization levels to determine the area's potential for growth, stabilization, or saturation.

[1] Market Segmentation

Demand for gaming can be classified into four primary categories: the local residents, tour and travel groups, leisure visitation, and convention visitation. Each of these gaming demand segments has distinct characteristics that affect the market's potential gaming revenues; these characteristics include gaming frequency, duration of play, gaming budgets, game preferences, and preferred facilities. With the exception of local residents, the demand generally originates from outside the subject property's primary market.

[a] Local Demand

In emerging riverboat, dockside, and Native American gaming markets, local residents constitute a significant portion of the overall gaming demand. The majority of patronage, an estimated 65 percent to 75 percent, originates within a fifty-mile radius. In such markets as Las Vegas and Atlantic City, which possess a critical mass of gaming, lodging, and entertainment facilities, local demand plays a secondary role to demand from the tour and travel, leisure, and convention segments. However, local patronage is necessary to provide a base level of annual demand, mitigating the effects of seasonality on revenues. In competitive markets, local patrons possess a high degree of loyalty, bas&d on personal service and incentives. Such incentives include complimentary food and beverage service, bonus winnings, complimentary room nights, complimentary travel, and gift items. Gaming frequency among local patrons depends on a number of factors, including the convenience of the casinos, the average age of the populace, and disposable income levels. Typically, local residents can be expected to allot a higher percentage of discretionary income to gaming activities than other demand segments. Locals often possess superior gaming skills and seek tables and devices that offer the highest payouts and best odds. In certain markets, locals tend to be seasonal in an attempt to circumvent the crowds associated with "peak" demand periods of tourist and leisure visitation.

[b] Tour and Travel Demand

The seasonality of tour and travel demand varies, depending on the type and mode of transportation. Demand generated by the tour and travel segment is primarily a function of an individual property's marketing efforts. While bus tours organized by outside wholesalers and recreational groups tend to be more seasonal, motor-coach tours, gaming junkets, and all-inclusive vacations marketed by the individual properties are booked in the shoulder and off-seasons to offset declining leisure visitation. The costs of marketing to this segment are high, and in some instances negate the potential gain in revenue. The primary goal in attracting tour and travel groups is gaming activity;
rooms and food and beverage outlets tend to be loss leaders. Gaming frequency among tour and travel patrons is high. Traditionally, tour and travel patrons favor gaming devices as opposed to table games. Depending on the type of group and predetermined gaming levels, tour and travel patrons allocate a considerable portion of their total travel budget for gaming activities and tend to make median-sized wagers per hand, or pull.

[c] Leisure Demand

Leisure visitation tends to be seasonal in nature, with visitors taking advantage of the favorable summer and spring seasons. Traditionally, the leisure segment uses both

table game and gaming devices, showing a higher propensity to play table games than the other demand segments. Gaming propensity and frequency within the leisure segment vary significantly, from "grind players," to "rated players." Further, the gaming budgets of leisure patrons vary considerably, as do their average wagers. While the primary goal in attracting the leisure traveler is gaming activity, food and beverage and retail outlets can also be priced to break even.

[2] Win per Unit per Day (WPUPD)

The win per unit per day (WPUPD) statistic provides the basis for the analysis and projection of table game and gaming device revenues. WPUPD is calculated by dividing total gaming revenues generated by a particular type of gaming unit by the number of gaming units available. Gaming statistics published in a majority of the gaming markets include the number of gaming units and total win figures by either table games and gaming devices or by individual games and devices (e.g., twenty-one tables, crap tables, five-cent devices, twenty-five-cent devices). The WPUPD provides insight into the efficiency of a market, demand levels, and saturation levels. In the forecast of gaming revenues, a WPUPD estimate is applied to the projected level of supply to arrive at an overall gaming win figure.

Like all other industries, gaming is subject to the laws of supply and demand. In open markets such as Mississippi and Las Vegas, supply can be expected to rise to a level supported by existing demand. During the initial growth phase, WPUPD levels are high, as the limited gaming inventory is insufficient to support high levels of pent-up demand. As new competition enters the market, demand is either dispersed among the competition, or the increase in inventory induces new demand to the market. The latter of the two scenarios will produce a stable WPUPD trend as demand increases at a rate equal to the increase in inventory. However, if demand is held constant or decreases, the result will be a declining WPUPD trend in the face of increasing inventory and competition. In addition, an entire market can be negatively affected by the emergence of a new gaming market proximate to the existing demand base. Through an analysis of the gaming market, an acceptable range of WPUPD levels can be derived and used to forecast marketwide gaming revenue.

Exhibit 23-7 presents an analysis of the hypothetical Cripple Stream gaming market. This analysis will be further used in the forecast of gaming win presented subsequently. Exhibit 23-8 presents an analysis of supply and demand trends in casinos.

The forecast of marketwide gaming win, presented in H 23.05, factors in the historical WPUPD levels attained by the market and the incremental change in WPUPD as inventory levels either increase or decrease. Additional factors affecting WPUPD levels are inflation, population growth, economic expansion, lodging supply, and tourism trends. The WPUPD estimates are then multiplied by the existing and proposed table game and gaming device inventory levels to arrive at a projection of marketwide gaming win.

» 23.05 FORECAST OF GAMING WIN

Once the subject market has been defined, and the supply and demand factors analyzed and quantified, the anticipated amount of gaming revenue generated by a specific casino operating within this market can be determined. The compilation of supply and demand data combined with research into the various external factors impacting an individual

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Exhibit 23-7 Analysis of Cripple Stream Gaming Market

		Tables and Games			Gaming Devices			
Year/Month	No. Casinos	Table WIN	Units	WPUPD	Device WIN	Units	WPUPD	Total WIN
1994								
January	13	$202,164	20	$326	$2,370,108	1,070	$71	$2,572,272
February	13	244,790	22	384	2,585,439	1,075	83	2,830,229
March	13	166,869	17	317	2,780,110	1,081	83	2,946,979
April	13	168,129	24	234	3,183,923	1,253	85	3,352,052
May	17	170,403	26	211	3,820,072	1,512	82	3,990,475
June	23	243,750	45	181	4,316,607	2,553	56	4,560,357
July	29	361,144	67	174	5,470,867	3,780	47	5,832,011
August	31	399,472	82	157	5,867,578	4,294	44	6,267,050
September	33	359,055	81	148	5,817,913	4,530	43	6,176,968
October	33	336,909	72	151	5,048,371	4,172	39	5,385,280
November	33	242,033	72	112	3,368,401	4,078	28	3,610,434
December	28	202,393	62	105	3,347,329	3,694	29	3,549,722
Total/Avg.		3,097,111	49	172	47,976,718	2,758	48	51,073,829
1995								
January	26	237,100	52	147	3,733,456	3,112	39	3,970,556
February	26	213,780	53	144	3,907,363	3,034	46	4,121,143
March	26	267,003	52	166	4,662,736	3,034	50	4,929,739
April	26	252,989	57	148	4,600,438	3,139	49	4,853,427
May	28	334,206	65	166	5,623,708	3,657	50	5,957,914
June	29	380,773	68	187	5,611,062	3,785	49	5,991,835
July	28	413,578	64	208	7,189,124	3,745	62	7,602,702
August	28	441,921	61	234	6,936,248	3,782	59	7,378,169
September	27	337,853	59	191	6,719,065	3,675	61	7,056,918
October	27	328,057	54	196	6,195,193	3,446	58	6,523,250
December	26	242,474	54	145	4,055,783	3,413	38	4,298,257
Total/Avg.		3,711,132	58	176	63,094,871	3,437	50	66,806,003
1996								
January	23	277,032	53	169	5,162,703	3,214	52	5,439,735
February	23	274,380	53	185	4,932,181	3,229	55	5,206,561
March	23	300,704	53	183	5,320,333	3,257	53	5,621,037
April	24	277,853	55	168	5,355,477	3,398	53	5,633,330
May	24	335,976	56	194	6,414,613	3,462	60	6,750,589
June	24	334,151	58	192	6,507,027	3,465	63	6,841,178
July	26	458,261	56	264	8,515,328	3,673	75	8,973,589
August	26	439,483	57	249	7,939,595	3,337	77	8,379,078
September	25	391,582	58	225	7,764,571	3,610	72	8,156,153
October	22	352,176	58	196	7,038,869	3,400	67	7,391,045
November	23	288,503	56	172	5,247,191	3,498	50	5,535,694
December	23	307,068	57	174	5,781,639	3,545	53	6,088,707
Total/Avg.		4,037,169	56	198	75,979,527	3,424	61	80,016,696

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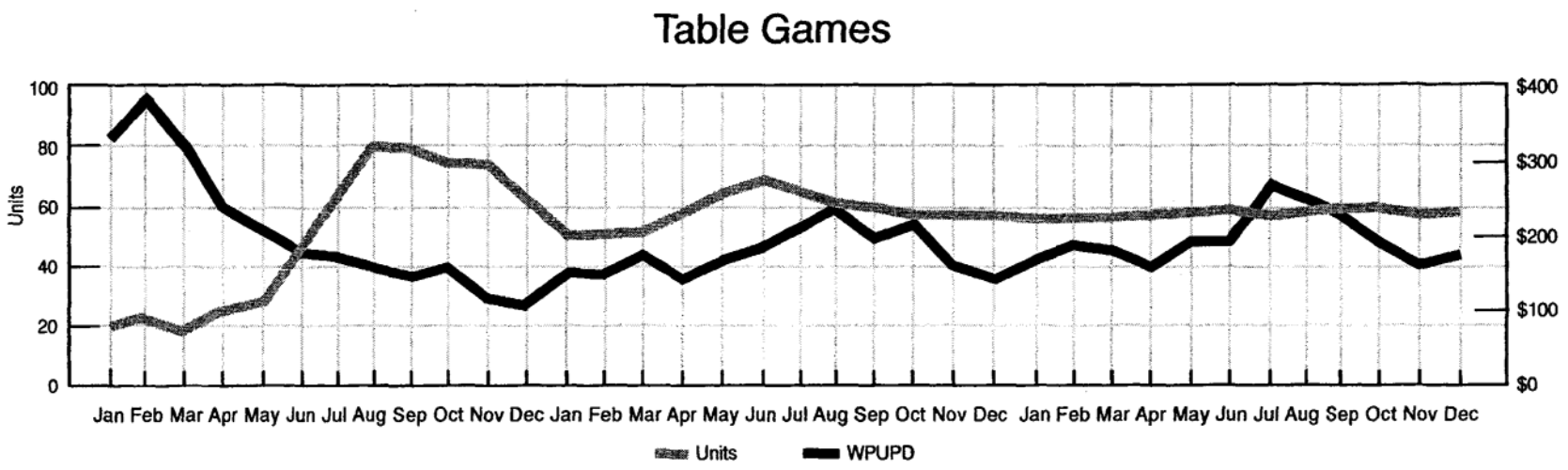
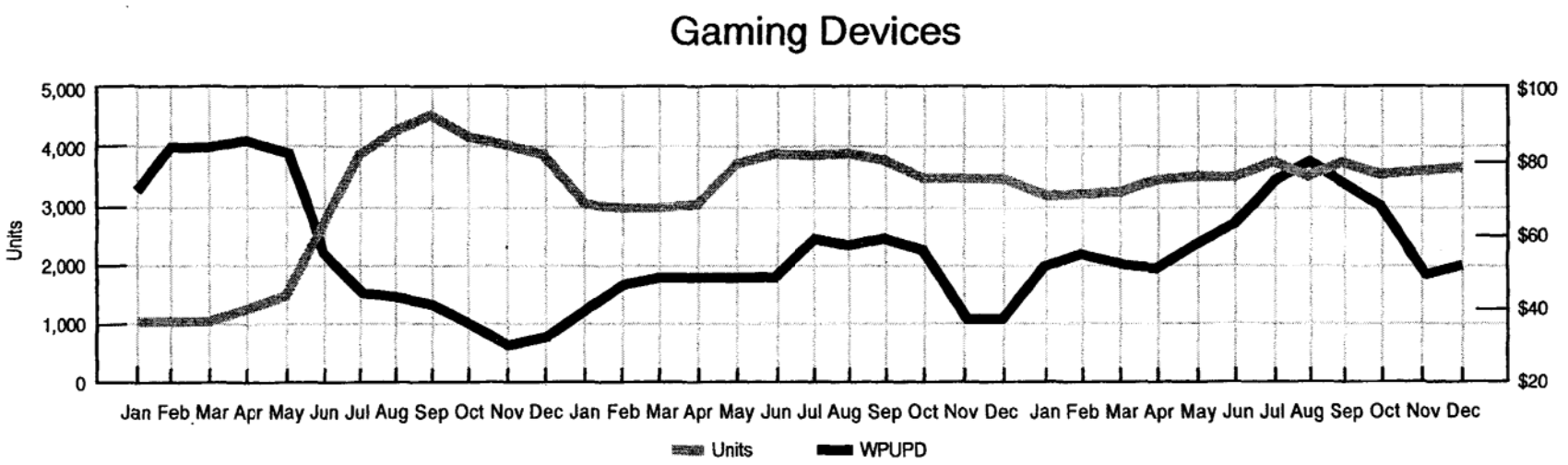
Exhibit 23-8 Analysis of Supply and Demand Trends





property's market share has led to the development of a market penetration model. Using the market derived data in the penetration model results in a forecasting tool that can be applied with a high degree of confidence. The market penetration model uses the following four steps in deriving a forecast of gaming revenue for the subject property.

1. The marketwide existing and proposed level of supply is quantified by table games and gaming devices throughout the projection period. The subject property's proposed level of supply is quantified by table games and gaming devices throughout the projection period. The subject property's fair share of marketwide gaming supply by table games and gaming devices is then calculated.
2. A forecast of marketwide gaming revenue is developed, based on the WPUPD and supply trends. Subjective factors such as latent demand levels, induced demand, and shifting demand patterns have been considered and included in the forecast of WPUPD levels and the resultant projection of marketwide gaming revenue.
3. Market penetration rates attainable by the subject property are projected for table games and gaming devices. The market penetration rates are then multiplied by the subject property's calculated fair share percentages to determine the subject's capture rate. The subject property's capture rate is then multiplied by the forecasted amount of marketwide gaming revenue, equating to the gaming revenue projected to be generated by the subject property.
4. The forecasted gaming win captured by the subject property is reconciled with a WPUPD analysis to check the reasonableness of the revenue projections. Combining the table game and gaming device win equates to an estimate of total gaming revenue.

[1] Step One—Fair Share

The subject property's fair share is calculated by dividing the subject's gaming inventory by the marketwide gaming inventory. For example, if the subject property has 100 table games and the total number of table games in the market, including the subject property, is 1,000, the subject property's fair share is equal to 10% (100 - 1,000 = 10 percent). Exhibit 23-9 shows projected marketwide gaming inventory and calculated fair share for the hypothetical Cripple Stream casino, as well as for a hypothetical Casino *X*.

[2] Step Two—Forecasting Marketwide Gaming Revenue

Step two involves the forecasting of marketwide gaming revenue in each year of the projection period. In order to minimize the effect of seasonality, the aggregate table game and gaming device win over a twelve-month period is used in the calculation of base year WPUPD. The base year table game WPUPD estimate is calculated as follows:

Table Game Win/Average Units/365 = WPUPD
$4,037,169/56/365 = $197.51 (rounded to $198)

On the basis of the historical WPUPD trend of the market, the incremental changes in gaming supply, and the anticipated impact of the new supply on the demand trends within the market, future WPUPD levels are estimated. The WPUPD figure is multiplied by the projected level of table game or gaming device inventory to arrive at a forecast of marketwide gaming revenue (see Exhibit 23-10).

Exhibit 23-9 Projected Marketwide Gaming Inventory and Calculated Fair Share

Table Games						
Gaming Inventory—Cripple Stream						
Existing Table Games	55	55	80	80	80	80
Additions to Supply	0	25	0	0	0	0
Total Table Games	55	80	80	80	80	80
Percent Change		45.5	0.0	0.0	0.0	0.0
Casino *X*						
Existing Table Games		25	25	25	25	25
Additions to Supply		0	0	0	0	0
Total Table Games		25	25	25	25	25
Calculated Fair Share-Table Games	31,3%	31.3%	31.3%	31,3%	31.3%	
Gaming Devices						
Gaming Inventory—Cripple Stream						
Existing Gaming Devices	3.500	3,500	4,500	4,750	4,750	4,750
Additions to Supply	0	1,000	250	0	0	0
Total Gaming Devices	3,500	4,500	4,750	4,750	4,750	4,750
Percent Change		28.6	5.6	0.0	0.0	0.0
Casino *X*						
Existing Gaming Devices	1,000	1,000	1,250	1,250	1,250	
Additions to Supply	0	250	0	0	0	
Total Gaming Devices	1,000	1,250	1,250	1,250	1,250	
Calculated Fair Share—Gaming Devices	22.2%	26.3%	26.3%	26.3%	26.3%	
Overall Fair Share	22.4%	26.4%	26.4%	26.4%	26.4%	

[3] Step Three—Projected Market Penetration Rates

Step three of the analysis includes projections of the subject property's market penetration rates. A penetration rate is defined as the percentage of marketwide gaming revenue the subject property will capture in relation to its fair share. For example, if the subject property's fair share of the marketwide gaming device inventory was 10 percent, and the property penetrates the gaming device segment at 110 percent, the subject would capture approximately 11 percent of marketwide gaming device revenue (1.10 x 0.10 = 0.11). The capture rate is then applied to the aggregate amount of marketwide gaming revenue to derive the subject property's gaming revenue forecast.

The forecast of market penetration rates attainable by the subject property must take into consideration the competitive advantages or disadvantages of the property, including location, visibility, accessibility, management, name recognition, historical operation, physical condition, and marketing (see Exhibit 23-11).

[4] Step Four—Projecting WPUPD

In step four, the projection of gaming revenue derived via the market penetration analysis is reconciled with a WPUPD analysis. Exhibit 23-12 presents estimated WPUPD projections for the subject property throughout the five-year projection period.

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Exhibit 23-10 Forecast of Marketwide Gaming Revenue—Cripple Stream Market

	Base Year	1997	1998	1999	2000	2001
Table Games						
Estimated WPUPD	$198	$175	$187	$192	$196	$200
Units	55	80	80	80	80	80
Total Win	$3,981	$5,109	$5,449	$5,620	$5,732	$5,847
Growth Rate		28.3%	6.7% ,	3.1%	2.0%	2.0%
Gaming Devices						
Estimated WPUPD	$53	$46	$45	$47	$48	$49
Units	3,500	4,500	4,750	4,750	4,750	4,750
Total Win	$67,381	$75,994	$77,542	$81,285	$82,911	$84,569
Growth Rate		12.8%	2.0%	4.8%	2.0%	2.0%
Total Gaming Win	$71,362	$81,103	$82,991	$86,905	$88,643	$90,416
Growth Rate		13.7%	2.3%	4.7%	2.0%	2.0%
Revenue Mix						
Table Games	5.6%	6.3%	6.6%	6.5%	6.5%	6.5%
Gaming Devices	94.4%	93.7%	93.4%	93.5%	93.5%	93.5%

Exhibit 23-11 Projected Penetration Rates and Captured Gaming Revenue

	1997	1998	1999	2000	2001
Total Gaming Win					
Table Games	$5,109	$5,449	$5,620	$5,732	$5,847
Gaming Devices	$75,994	$77,542	$81,285	$82,911	$84,569
Total Gaming Win	$81,103	$82,991	$86,905	$88,643	$90,416
Estimated Penetration Factors					
Table Games	110.0%	110.0%	115.0%	120.0%	120.0%
Gaming Devices	120.0%	125.0%	130.0%	130.0%	130.0%
Overall	121.4%	125.0%	130,0%	130.4%	130.4%
Captured Gaming Win					
Table Games	$1,760	$1,870	$2,020	$2,150	$2,190
Gaming Devices	$20,270	$25,510	$27,810	$28,360	$28,930
Total	$22,030	$27,380	$29,830	$30,510	$31,120
Percentage Change					
Table Games		6.3%	8.0%	6.4%	1.9%
Gaming Devices		25.9%	9.0%	2.0%	2.0%
Total		24.3%	8.9%	2.3%	2.0%
Revenue Mix					
Table Games	8.0%	6.8%	6.8%	7.0%	7.0%
Gaming Devices	92.0%	93.2%	93.2%	93.0%	93.0%

Exhibit 23-12 Projected WPUPD and Total Gaming Win					
	1997	**1998**	**1999**	**2000**	**2001**
Table Games					
WPUPD	$193	$205	$221	$236	$240
Units	25	25	25	25	25
Win	$1,760	$1,870	$2,020	$2,150	$2,190
Gaming Devices					
WPUPD	$56	$56	$61	$62	$63
Units	1,000	1,250	1,250	1,250	1,250
Win	$20,270	$25,510	$27,810	$28,360	$28,930
Total Gaming Win	$22,030	$27,380	$29,830	$30,510	$31,120
Growth Rate		24.3%	8.9%	2.3%	2.0%

» 23.06 DISTANCE-BASED VISITATION MODEL—RIVERBOAT CASINOS

The current and projected trends in economic and demographic factors such as population base, employment trends, disposable income levels, and visitation statistics have a direct impact on a market's demand for gaming facilities. Forecasting potential casino visitation becomes a function of this economic and demographic data as well as specific information pertaining to the gaming habits and preferences of a particular market's populace. General data on penetration rates and trip frequencies within certain geographical areas have been compiled by the research departments of several leading gaming companies. The compilation of this data has led to the development of a distance-based visitation model, which uses the following four steps in deriving a forecast of marketwide casino visitation.

1. Identify the subject market's capturable base population by using a concentric-circle analysis. The sizes of the concentric circles are typically 0-50 radial miles, 50-100 radial miles, and 100-150 radial miles. In addition to identifying and quantifying the capturable base population, the current level of visitation from outside the 150-mile radius is quantified.
2. Growth rates are applied to the capturable base population figures over the estimated projection period. In addition, an overlap adjustment is applied to the base population estimates within each of the concentric circles to account for regional competition. Similar to the population estimate, a growth rate is applied to the base visitation estimate over the projection period. Finally, the incremental level of visitation generated by the opening of the subject property or other gaming facilities is quantified.
3. Penetration and trip frequency rates are projected for each of the concentric circles, the current visitation levels, and the incremental visitation levels. The rates are then multiplied to derive the gaming incidence factor specific to each concentric circle and visitation segment. The gaming incidence factor is then multiplied by the adjusted base population estimate for each concentric circle and both visitation estimates, equating to the projected number of casino visits within the market.

4. The subject property's fair share, market penetration, and market capture rates are then estimated and applied to the projected number of accommodated casino visits within the market to arrive at the projected number of casino admissions at the subject property.

[1] Step One—Concentric Circle Analysis

Three concentric circles are plotted around the subject property. The circles represent the primary local market within a 50-mile radius of the subject property, the secondary market from 50 to 100 miles, and the tertiary market from 100 to 150 miles. The primary market includes local residents who tend to have a higher propensity to gamble because of the convenience of the casino facility. For the same reason, the local market also generates a higher average trip frequency figure. The secondary market, while viable, can be subject to regional competition depending on the proximity of the subject property to competitive gaming markets and its relative accessibility from primary transportation routes. An additional factor affecting the secondary market is the marketing campaign employed by management. The tertiary market is composed of "day trippers," who often have a choice between gaming locations of equal distance given the location of the subject property. The tertiary market necessitates the highest overlap adjustment and the lowest penetration and trip frequency estimates.

Exhibit 23-13 delineates the derived base population figures, the capturable adult population, and the current adult visitation level.

Exhibit 23-13 Estimated Base Population and Visitation Levels (OOOs)

Data Type	0-50 Miles	50-100 Miles	100-150 Miles	Total
Base Population (000)	1,057.3	1,735.3	556.8	3,349.4
Percent of Populace Over 21	75.0%	75.0%	75.0%	75.0%
Capturable Adult Population (000)	793.0	1,301.5	417,6	2,512.1
Plus: Estimated Adult Visitation				4,600.0
Total Capturable Adult Population				7,112.1

[2] Step Two—Forecasting Adjusted Capturable Population and Visitation

On the basis of the area's population statistics, an annual growth rate is applied to the capturable population figures. Similarly, a growth rate is applied to the current visitation levels, reflecting the area's tourism and convention climate. Incremental visitation as a result of the subject casino's opening is projected to decrease by 50 percent in the second year and cease in the third year of the projection period. Overlap adjustments have been applied to each of the concentric circles in order to account for the lost visitation due to the proximity of regional competitive gaming markets. The overlap adjustments are then applied to the capturable population projections to arrive at an adjusted capturable population estimate. Exhibit 23-14 presents the capturable population base, applied growth rates, and overlap adjustments resulting in a forecast of adjusted capturable population and visitation.

Exhibit 23-14 Base Population and Visitation Levels, Applied Growth Rates, and Overlap Adjustments (000s)

	Base Year	1997	1998	1999	2000	2001
Capturable Population and Visitation Levels						
Capturable Population Growth Rates		0.5%	0.5%	0.5%	0.5%	0.5%
0–50 Miles	793	801	805	809	813	817
50–100 Miles	1,301	1,315	1,321	1,328	1,334	1,341
100–150 Miles	418	422	424	426	428	430
Subtotal	2,512	2,537	2,550	2,563	2,576	2,588
Overlap Adjustment						
0–50 Miles		0.10	0.10	0.10	0.10	0.10
50–100 Miles		0.40	0.40	0.40	0.40	0.40
100–150 Miles		0.90	0.90	0.90	0.90	0.90
Adjusted Capturable Population						
0–50 Miles		721	724	728	732	725
50–100 Miles		789	793	797	801	805
100–150 Miles		42	42	43	43	43
Subtotal		1,552	1560	1,567	1,575	1,583
Visitation Growth Rate		0.5%	0.5%	0.5%	0.5%	0.5%
Current Visitation	4,600	4,646	4,669	4,693	4,716	4,740
Incremental Visitation Growth Rate			(50.0%)	(100.0%)	0.0%	0.0%
Incremental Visitation		50	25	0	0	0
Total Population and Visitation	7,112	7,234	7,244	7,256	7,292	7,328

[3] Step Three—Projecting Casino Visits Within the Market

Step three includes the forecast of penetration rates and trip frequency factors equating to a gaming incidence factor. A penetration rate is defined as the percentage of capturable population in each market segment that is projected to visit a casino at least once annually. Trip frequency is defined as the average number of visits per annum. A penetration rate of 60 percent and a trip frequency of 7.0 equates to a gaming incidence factor of 4.2 (.60 x 7.0 = 4.2). The gaming incidence factor is then applied to the adjusted capturable population and visitation levels to derive the projected number of annual casino visits to the subject's market area.

Based on the various sources, penetration rates range from 50 percent to 70 percent within primary markets, from 25 percent to 50 percent within secondary markets, and from 10 percent to 35 percent within tertiary markets. Trip frequencies range from 3.0 to 7.0 within a 50-mile radius, 1.5 to 4.0 from 50 to 100 miles, and 1.0 to 3.0 from 100 to 150 miles. Exhibit 23-15 presents calculated gaming incidence factors and projected annual casino visits throughout the projection period.

[4] Step Four—Projecting Casino Admissions

Step four of the analysis includes the calculation of the subject property's fair share, and projection of market penetration rates equating to the overall estimate of casino admissions captured by the property. The subject property's fair share is calculated by

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Exhibit 23-15 Calculation of Gaming Incidence Factor and Projected Annual Casino Visits

	1997	1998	1999	2000	2001
Projected Penetration Rates					
0-50 Miles	0.48	0.48	0,48	0.48	0.48
50-100 Miles	0.40	0.40	0.40	0.40	0.40
100-150 Miles	0.30	0.30	0.30	0.30	0.30
Current Visitation	0,40	0.40	0,40	0.40	0.40
Incremental Visitation	1.00	1.00	N/A	N/A	N/A
Estimated Trip Frequency					
0-50 Miles	7.00	7.00	7,00	7.00	7.00
50-100 Miles	4.00	4.00	4.00	4.00	4.00
100-150 Miles	2.00	2.00	2.00	2.00	2.00
Current Visitation	1.00	1.00	1.00	1.00	1.00
Incremental Visitation	1.00	1.00	N/A	N/A	N/A
Gaming Incidence Factor					
0-50 Miles	3.36	3.36	3.36	3.36	3.36
50-100 Miles	1,60	1.60	1.60	1.60	1.60
100-150 Miles	0.60	0.60	0.60	0.60	0.60
Current Visitation	0.40	0.40	0.40	0.40	0.40
Incremental Visitation	1.00	1.00	N/A	N/A	N/A
Projected Annual Casino Admissions—Marketwide (000)					
0-50 Miles	2,422	2,434	2,446	2,459	2,471
50-100 Miles	1,262	1,268	1,275	1,281	1,287
100-150 Miles	25	25	26	26	26
Current Visitation	1,858	1,868	1,877	1,887	1,896
Incremental Visitation	50	25	0	0	0
Total	5,618	5,621	5,624	5,652	5,680
Growth Rate		0.1%	0.1%	0.5%	0.5%
Unaccomodated Demand Adjustment					
Weekly and Seasonal Fluctuations	5.0%	5.0%	5.0%	5.0%	5.0%
Accomodated Casino Admissions					
0-50 Miles	2,301	2,312	2,324	2,336	2,347
50-100 Miles	1,199	1,205	1,211	1,217	1,223
100-150 Miles	24	24	24	24	25
Current Visitation	1,766	1,774	1,783	1,792	1,801
Incremental Visitation	50	25	0	0	0
Total	5,339	5,341	5,342	5,369	5,396

dividing the subject's estimated capacity, expressed as the casino square footage, by the marketwide capacity. For example, if the subject property's casino is 30,000 square feet and the total capacity of the market, including the subject property, is 100,000 admissions per day, the subject property's fair share is equal to 30% (30,000 - 100,000 = 30 percent).

A penetration rate is defined as the percentage of marketwide gaming visitation the subject property will capture in excess of its fair share. For example, if the subject property's fair share of the marketwide capacity was 30 percent, and the property was projected to penetrate the market at 110 percent, the subject would capture approximately 33 percent of marketwide visitation (1.10 X 0.30 = 0.33). The capture rate is then applied to the aggregate amount of marketwide visitation to derive the subject property's admissions forecast.

Penetration into the market reflects a variety of factors including accessibility, available parking, visibility, and proximity to population centers, lodging supply, and tourist attractions. Second, the design and layout of the riverboat complex has a direct impact on visitation. Finally, management's expertise in marketing, customer data base, and name recognition all affect casino visitation.

Exhibit 23-16 presents the subject property's calculated fair share percentages, projected penetration rates, and captured gaming admissions throughout the five-year projection period.

Exhibit 23-16 Estimated Market Capture and Projected Number of Admissions

	1997	1998	1999	2000	2001
Marketwide					
Existing Capacity (Square Footage)	195,000	195,000	195,000	195,000	195,000
Additions to Supply	0	0	0	0	0
Total	195,000	195,000	195,000	195,000	195,000
Percentage Change	0.0	0.0	0.0	0.0	0.0
RIverboat Casino					
Existing Capacity (Square Footage)	30,000	30,000	30,000	30,000	30,000
Additions to Supply	0	0	0	0	0
Total	30,000	30,000	30,000	30,000	30,000
Calculated Fair Share	15.4%	15.4%	15.4%	15.4%	15.4%
Estimated Penetration Rate	100.0%	105.0%	110.0%	110.0%	110.0%
Calculated Market Share Rate	15.4%	16.2%	16.9%	16.9%	16.9%
Projected Admissions—RIverboat Casino (000)					
0-50 Miles	354	374	393	395	397
50-100 Miles	184	195	205	206	207
100-150 Miles	4	4	4	4	4
Current Visitation	272	287	302	303	305
Incremental Visitation	8	4	0	0	0
Total	821	863	904	909	913
Percentage Change		5.0	4.8	0.5	0.5

[5] Forecasted Win per Admission

A forecast of aggregate gaming win generated by the market and the subject property can be derived by multiplying the forecasted casino visitation statistics by an estimated win per admission figure. The following is a step-by-step analysis of win per admission levels:

- A survey of comparable facilities operating within similar gaming markets is performed to determine average wagers and average duration of play for both table game and gaming device patrons.
- These estimates are multiplied by the average number of decisions per hour and the weighted house advantage for both table games and gaming devices to determine a respective win per admission figure.
- The estimated table game and gaming device win per admission figures are then weighted by each segment's typical contribution to total gaming revenue. Our analysis of comparable gaming markets indicates that table game revenues contribute approximately 20 percent of total gaming win, while gaming device revenues contribute the remaining 80 percent of total gaming win.
- The two weighted win per admission estimates are summed, equating to an overall win per admission figure.

Exhibit 23-17 Forecasted Win per Admission

Table Game Patron		Gaming Device Patron	
Average Wager	$10.00	Average Wager	$0.75
Average Duration of Play (hours)	3	Average Duration of Play (hours)	3
Decision per hour	55	Decision per hour	240
House Advantage	1.80%	Hold Pecentage	7.0%
Average Win per Admission	$29.70	Average Win per Admission	$37.80
Percentage of Total Win	20		80%
Weighted Average Win per Admission	$5.94		$30.24
Overall Win per Admission	$36.18		

Exhibit 23-17 presents the first-year forecast of overall win per admission. The variables used in the analysis reflect both industry averages and estimates specific to the market. Variables such as decisions per hour and the house advantage are industry standards, while the average wagers and duration of play estimates are based on comparable market activity and discussions with local operators. Estimated average table game wagers reflect the changes in minimum wagers set by the house as a function of peak and off peak demand periods. The duration of play is based on an average excursion times, including embarkation and disembarkation. Average wagers for gaming devices reflect the estimated predominance of reel machines, which allow a maximum drop of three coins per pull. Video poker and progressive video poker machines generally allow a maximum drop of five coins per pull but are anticipated to account for only a moderate portion of the overall device inventory. Gaming devices hold percentages are based on industry averages reflecting the level of competition and marketwide demand

levels. Reflecting a stable supply of gaming inventory, economic, demographic, and inflationary growth within the market, a 1.0 percent average annual growth rate has been applied to win per admission figures throughout the projection period.

Applying the win per admission estimates to the projected gaming admissions captured by the subject property equates to the forecasted gaming revenue anticipated to be generated throughout the five-year period (see Exhibit 23-18).

Exhibit 23-18 Forecasts of Marketwide Gaming Revenue and Subject Property's Gaming Revenue

	1997	1998	1999	2000	2001
Forecast of Marketwide Gaming Revenue					
Forecasted Admissions	5,617,843	5,620,682	5,623,660	5,651,779	5,680,037
Win per Admission	$36.18	$36,90	$37,64	$38.39	$39.16
Marketwide Gaming Win	$203,253,547	$207,423,395	$211,683,976	216,997,243	$222,443,874
Rounded	$203,300,000	$207,400,000	$211,700,000	$217,000,000	$222,400,000
Growth Rate		2.0%	2.1%	2.5%	2.5%
Forecast of Subject Property's Gaming Revenue					
	1997	**1998**	**1999**	**2000**	**2001**
Forecasted Admissions	821,454	862,760	904,112	908,632	913,175
Win per Admission	$36.18	$36.90	$37.64	$38.39	$39.16
Total Forecasted Gaming Win	$29,720,203	$31,838,965	$34,032,270	$34,886,480	$35,800,000
Growth Rate		7.1%	6.9%	2.5%	2.5%

HVS

CHAPTER 24

Selecting a Consulting and Appraisal Firm

¶ 24.01 The Impact of FIRREA 24-1
¶ 24.02 Basic Requirements 24-2
¶ 24.03 Initial Selection Process 24-3
¶ 24.04 Firm Qualifications Checklist 24-3
¶ 24.05 Assignment Proposal 24-4

» 24.01 THE IMPACT OF FIRREA

The 1990s brought about significant change in the hotel appraisal and consulting industry. During the 1980s, the deregulation of savings and loans led many uninformed lenders to finance commercial real estate projects, including hotels, that were not economically viable. Other commercial lenders followed suit, and the commercial real estate markets became greatly overbuilt. The resultant demise of numerous savings and loans and commercial banks led to the passing of the Financial Institutions Reform and Recovery Enforcement Act (FIRREA), which went into effect in August, 1990. The bill called for stricter regulation of lenders, which in turn helped lead to the capital crunch for commercial real estate from mid-1990 through 1993.

Prior to the enactment of FIRREA, hotel developers interested in obtaining mortgage financing used the following procedure. First they would bring their proposal to a lender, whose usual response was to request that the developer have a feasibility study prepared by one of the major accounting firms with an active hotel accounting practice. After thirty to sixty days, the developer would deliver this study to the lender. The study would often have a bias in favor of the developer and his or her project, because the consultant was being directed and paid by the developer. If, after reviewing the study, the lender wanted to proceed, the developer would be told that an appraisal performed by a member (MAI) of the American Institute of Real Estate Appraisers (now known as the Appraisal Institute) was required to justify the amount of the loan. The developer could then hire the appraiser directly. A generalist appraiser who did not understand the hotel industry was often hired to "cap" the forecast of net income set forth in the feasibility analysis. Cost and sales comparison approaches were added to the analysis and the appraisal was complete. Only after another twenty to thirty days had passed and additional fees were paid would the developer have finally satisfied the lender's requests for market and financial analyses and valuation.

Some firms developed the in-house expertise to develop a combined economic study and appraisal that contained all the components of a feasibility study as well as those of an appraisal. This product reduced the cost and time of the process, but no matter how the due diligence was undertaken, the developer was always in control of the process and often pressured the consultants and appraisers to be overly optimistic. One of the most significant changes brought about by the FIRREA legislation was the requirement that any federally insured financial institution had to directly hire the appraiser for the financing of a piece of real estate. The developers and owners looking to build, finance a purchase, or refinance an existing asset were removed as the middleman in the appraisal process. This legislation lifted the pressure to "make a number" that appraisers and consultants previously had to deal with.

FIRREA had many drawbacks, including regulations so strict that lenders became paralyzed in the lending process and were forced to write down any underse-cured loans and to foreclose on borrowers who could not come up with the additional equity to meet regulated loan-to-value requirements. The restrictive lending environment led to a shortage of capital for refinancing and healthy economic activity, and financial institutions and the real estate industry eventually spoke up about the regulation that helped exacerbate the economic downturn of the early 1990s. The interpretation of FIRREA began to loosen up in 1993, and the remnants of the legislation that remain with us today are generally conducive to a healthy and prudent lending environment.

FIRREA also resulted in the requirement that any appraisal performed for a fed-erally insured real estate transaction must be performed by a state-certified appraiser. State certification is the minimum level of qualification that should be expected from professional appraisers. The requirements to become an MAI are significantly greater than those required to become state certified, but the law requires that a federally insured lender must not discriminate against an individual who does not hold a professional designation such as the MAI. Lenders are, however, permitted to retain the most qualified appraiser, which is generally someone holding the MAI designation.

» 24.02 BASIC REQUIREMENTS

The key to obtaining a report that will fulfill the lender's requirements for both feasibility analysis and appraisal is twofold; (1) select a qualified hotel consulting and appraisal firm, and (2) provide that firm with detailed instructions regarding the specific issues that must be addressed in the study and the format that the final report should take,

Choosing the wrong consulting and appraisal firm to perform a market study and appraisal can be a costly mistake. A market study and appraisal of a lodging facility requires in-depth knowledge of hotel markets and operations; the consulting firm that is chosen should be staffed by either hotel management school graduates or consultants with extensive on-the-job hotel operating experience. Similarly, the appraiser who works on the project should have a hotel management background to ensure that he or she thoroughly understands the unique dynamics of hotel market studies and appraisals.

Some consulting firms try to integrate the work of market consultants trained by hotel schools with that of appraisers with general real estate backgrounds. In such cases, the market study portion is usually performed by the hotel expert, who also prepares the financial projections. The appraiser then capitalizes the resulting net income and renders an opinion of value. This division of responsibility does enable these firms to perform hotel market studies and appraisals, but difficulties frequently arise with the coordination of professionals possessing divergent areas of expertise.

As a result, the final product is too often a compromise of conclusions. The lodging industry is complex and constantly changing, which means that specialists who concentrate all their efforts within the field are best suited to conduct market studies and appraisals for this market.

» 24.03 INITIAL SELECTION PROCESS

The key to choosing the best company to undertake a study is to look beyond the prestige of the firm and concentrate instead on the abilities of the personnel that will actually produce the study. When first assembling a list of candidates to perform a market study or to recommend to a lender for an appraisal, the developer must make sure that limiting conditions are clearly understood. Many firms will not allow their reports to be used in any form of public or private offering, which can seriously impair the utility of a study. The developer should also beware of firms that isolate or limit interaction with any of the personnel working on the study. Starting with the first meeting and with every meeting thereafter, all members involved with the project should be in attendance. This personal interaction is necessary for everyone to be as familiar as possible with the concepts behind the project and to fully share the combined knowledge, experience, and insights of the team.

» 24.04 FIRM QUALIFICATIONS CHECKLIST

The selection of a consulting and appraisal firm requires a thorough evaluation of each prospective firm's expertise and credibility. The following checklist is a useful means of determining whether a company is able to conduct a proper market study and appraisal.

° *Does the firm operate on a national level? Does it have strong regional expertise?* Exposure to many types of markets enhances the level of expertise, while regional expertise deepens the knowledge of particular markets. A local firm may be handicapped in its knowledge of various lodging products and how they perform under different market conditions. A national firm with regional expertise often provides the best of both worlds.

° *Does the firm use hotel-trained personnel for both the market study and appraisal portions of the study?* A study of this type should not be divided between market study consultants and appraisers, particularly if the appraisers have no specific expertise in hotel operations.

° *Does the firm have specialized expertise in hotel-related studies?*

° *Who will be working on the assignment?* Copies should be obtained of the consultants' and appraisers' qualifications, background, and experience. Since a hotel is a highly specialized business venture, it is essential to meet with the appraisers, including the state-certified MAI who will be working on the assignment, to determine whether each individual has the following minimum qualifications;

- A degree from an accredited hotel management school;
- Actual operating experience in the hospitality industry;
- Postgraduate courses in real estate principles and practices, real estate appraisal, and real estate finance; and

• Experience in evaluating a wide range of lodging facilities, both proposed and existing.

° *Does the firm have the high level of credibility necessary to defend its conclusions in the event they are questioned?* This issue is especially important. Generalists who devote time to other types of real estate have difficulty staying current with industry data, statistics, and trends. True experts tend to publish widely in professional journals and to be active as lecturers in the field. If the most qualified expert is sought out to perform a hotel market study and appraisal, the client will be assured of receiving a high-quality, reputable product.

» 24.05 ASSIGNMENT PROPOSAL

After a qualified hotel consulting and appraisal firm has been selected, the next step is to ascertain the fee the firm will charge and the time it will need to complete the study. The right approach at this early stage can often save money. Usually, the officer or partner in charge of the appraisal practice is contacted by phone to discuss the potential assignment. At this point, the developer should discuss the nature and scope of the project. All the details and issues of the project and assignment should be clarified up front so that the consultant can quote a fair fee for all the work that will be involved and so that the developer will not face any unanticipated fees on the conclusion of the assignment.

While the developer may have already prepared an in-house analysis of the market and the feasibility of a project, he should not expect the consultant to reduce his or her fee quote. Good consultants and appraisers will have to perform their own primary research in performing a market study or appraisal, and any attempt to reduce either the time they spend or the resultant fee may end up causing more trouble than it is worth in the long run.

If the developer is planning to build several hotels, it is a good idea to tell the appraiser before determining the fee. In addition, the fee might be reduced if the developer is willing to wait for the appraisal until a time that is convenient for the appraiser. It is important to remember, however, that quality generally corresponds to price. It is worthwhile to make an effort to reduce costs, but not at the expense of the careful selection of the most qualified firm possible. The time and money spent to secure a capable firm that will produce an accurate study will be recouped in the future, because the myriad decisions involved in the development or acquisition of a lodging facility will be based on a thoroughly researched and soundly reasoned study.

The developer should ask for an all-inclusive fee that comprises professional and computer time charged, report production costs, and miscellaneous expenses (e.g., telephone, postage, and photocopying). It is best, however, to reimburse out-of-pocket travel expenses on the basis of actual receipt invoices rather than a lump-sum estimate. Beware of firms that bill travel expenses at a rate higher than their actual cost. Finally, expect to pay a sizable retainer fee before work commences.

After preliminary discussions regarding the objectives of the assignment, a capable consultant should be able to present a detailed document outlining what steps will be taken to provide the services discussed. The proposal is actually a contract in letter form, outlining the services to be rendered and fees charged. Once the contract has been signed and returned by the developer, the valuation company is usually given forty-five to sixty days to complete the assignment.

A proposal that does not appear to adequately address any of your specific needs or concerns may be an indication that the consultant has not grasped what you are

looking for. This is the time to have another discussion with the consultant or to find an alternate prospect to perform the work. Preparing a formal request for proposal (RFP) containing specifications for the assignment is not recommended in this age of time and fee constraints. Many excellent consultants and appraisers will not respond to an RFP because they do not believe that the potential client has taken the time to narrow the field of competition to truly qualified players. Responding to an RFP can be time consuming, and the good consultants are often too busy to reply.