Las Vegas Casino & Hotel Market Outlook 2009

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January 2009

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Any previously held notion that the Las Vegas gaming-tourism industry is recession-proof was dispelled in 2008 as, to quote the Las Vegas Review Journal, *"the imploding economy drove a stake though the heart of the Strip." The downturn in the national and worldwide economies, and the resulting decrease in consumer consumption, has reduced visitation to the Las Vegas market in 2008 to levels not seen since 2004, which was prior to the opening of major properties including the Wynn Las Vegas, South Point, Red Rock Station, Palazzo, and Encore. As quality new supply is absorbed and operators have implemented strategies to compete for overnight guests to support gaming and other amenities, average daily room rate has dropped. The recession is prompting visitors and locals to gamble less. Challenging economic conditions, including the turmoil in the credit markets, have also resulted in a scaled-back development pipeline. Ultimately, Las Vegas' recovery is not expected until economic conditions improve and the resulting resumption of consumer confidence and spending.*

The economic driver of Las Vegas[1] is obviously tourism and related service sectors. In addition to tourism, Las Vegas' economic base continues to diversify into areas such as manufacturing, distribution, wholesale trade, and construction. While these sectors have emerged within Las Vegas, the area's driving force is, and will continue to be, gaming-related tourism, which is highly dependent upon consumer confidence and spending.

Visitation

Las Vegas has a long history of consistent growth. Las Vegas has been experiencing year-over-year increases in the total number of visitors since 2002, growing to roundly 39,200,000 visitors in 2007. The only annual decline in visitation in the period from 1990 to 2007 (2.3%) was a result of the terrorist attacks in 2001. Visitation to Las Vegas increased at an average annual compounded rate of change of 1.9% for the period from 2001 to 2007. Table 1 depicts the number of visitors to Las Vegas from 1990 through November 2008 based on data from the Las Vegas Convention and Visitors Authority (LVCVA).[2]

New gaming and hotel supply, entertainment, attractions, and other amenities have historically provided an impetus for increased visitation. The development of must-see properties, attractions, and amenities, including the Luxor, Treasure Island, and MGM Grand Hotel, in 1993 contributed to the

Table 1 – Las Vegas Visitors

Year	Total Visitors	% Change
1990	20,954,420	---
1991	21,315,116	1.7 %
1992	21,886,865	2.7
1993	23,522,593	7.5
1994	28,214,362	19.9
1995	29,002,122	2.8
1996	29,636,361	2.2
1997	30,464,635	2.8
1998	30,605,128	0.5
1999	33,809,134	10.5
2000	35,849,691	27.1
2001	35,017,317	(2.3)
2002	35,071,504	0.2
2003	35,540,126	1.3
2004	37,388,781	5.2
2005	38,566,717	3.2
2006	38,914,889	0.9
2007	39,196,761	0.7
Year-to-date through November:		
2007	36,120,930	---
2008	34,741,853	(3.8)
Average Annual Compounded Change, 1990-2007:		3.8 %
Average Annual Compounded Change, 2001-2007:		1.9 %

Source: Las Vegas Convention & Visitors Authority

[1] Las Vegas is located in Clark County, Nevada.

[2] Note that Las Vegas visitor data for December 2008 is not available as of the date of this article.

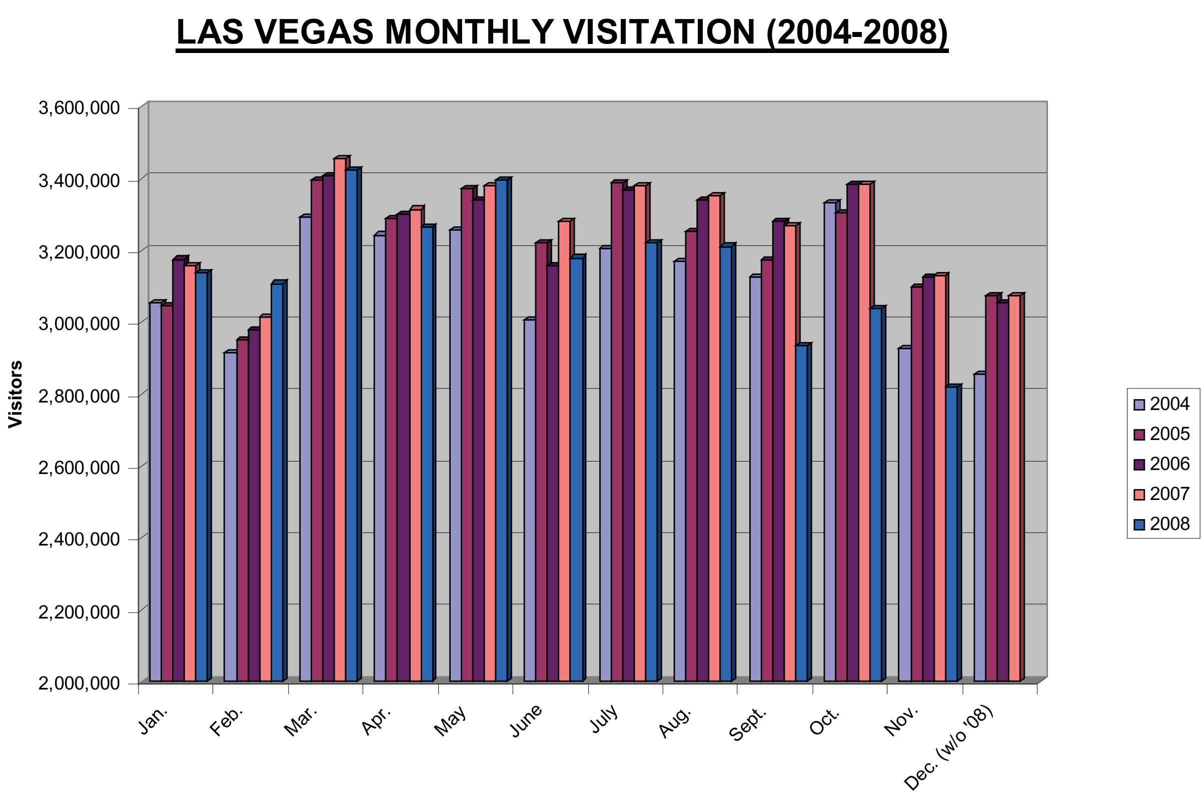
19.9% increase in visitors in 1994 and was a clear indication that Las Vegas was transitioning from a solely gaming-based orientation. The major wave of expansion that began in 1998, which included the opening of the Bellagio, Mandalay Bay, Paris Las Vegas, Venetian, and Planet Hollywood (previously known as the Aladdin), contributed to the 10.5% increase in visitors in 1999 and 27.1% increase in 2000. These developments have increased gaming demand and changed the overall revenue mixture from primarily gaming to a more balanced distribution between gaming, hotel, retail, and entertainment. However, as a result, the market has become more susceptible to downturns in the economy and declining consumer consumption.

Year-to-date data through November 2008 clearly indicates that the largest year-over-year decline in total visitation to Las Vegas over the time frame examined was experienced in 2008. Through November 2008, there were nearly 1.4 million fewer visitors than during the same period in 2007, a decline of 3.8%. In November 2008, the latest month for which data is currently available, visitation to Las Vegas was down 9.8% compared to November 2007. Chart 1 sets forth the number of monthly Las Vegas visitors over the last four years.

As indicated in Chart 1, the number of visitors to Las Vegas on a monthly basis during the first half of 2008 was relatively comparable to that in 2006 and 2007. However, the number of visitors from California, a major feeder market for Las Vegas, began to decline as gas prices reached record heights during the summer and as the economic downturn worsened through the year; the number of visitors during the months of September, October, and November 2008 were 10.1%, 10.2%, and 9.8% lower, respectively, than during the same months in 2007. As indicated in Chart 1, the number of visitors during these three months was less than visitation during the same three months in 2004.

While the major developments currently in the

Chart 1 - Las Vegas Monthly Visitation (2004-2008)



pipeline, including MGM's CityCenter, may drive additional visitation, it is unlikely that the growth in visitation will reach double digits as in 1994, 1999, and 2000 due to the prevalence of available gaming alternatives nationwide and throughout the world. Since 2004, several quality properties have opened in Clark County, including the Wynn Las Vegas in April 2005, South Point (previously known as South Coast) in December of 2005, Red Rock Station in April 2006, Palazzo in December 2007, and Encore in December 2008. The fanfare and increased visitation upon the opening of these properties have been noticeably insignificant relative to that experienced during previous waves of development.

Lodging Demand

Historically, the Las Vegas lodging market attained occupancy levels well above the national average due to the need for casino operators to fill their rooms at a market-driven price point in order to generate patrons for their casinos. Hotel occupancy has historically been higher than motel occupancy and has been over 90% since 2004. Growth in lodging demand has historically been a function of new supply and resulting visitation, as evidenced by the increases in occupied rooms of 17.4% in 1993, 13.0% in 1996, and 12.8% in 1999. Table 2 presents Las Vegas lodging market statistics from 1990 through 2007 and the year-to-date periods through November 2007 and 2008.

As presented in Table 2, available inventory and occupied rooms increased at average annual compounded rates of 0.4% and 1.0%, respectively, between 2004 and 2007. Overall, total occupancy remained relatively stable during this time.

As previously indicated, several quality properties have opened since 2004, including the Wynn Las Vegas, South Point, Red Rock Station, Palazzo, and Encore. Additionally, the Stardust closed in 2006. In the period from 2004 to 2007, average daily rate increased at an average annual compounded rate

Table 2 - Analysis of Las Vegas Lodging Statistics

Year	Inventory	% Change	Total Rooms Occupied	% Change	Hotel Occupancy	Motel Occupancy	Total Occupancy	Overall ADR	% Change
1990	73,730	---	22,793,998	---	89.1 %	69.8 %	84.7 %	N/A	
1991	76,879	4.3 %	22,532,851	(1.1) %	85.2	62.6	80.3	N/A	
1992	76,523	(0.5)	23,434,021	4.0	88.8	66.1	83.9	N/A	
1993	86,053	12.5	27,514,586	17.4	92.6	69.7	87.6	N/A	
1994	88,560	2.9	28,768,716	4.6	92.6	73.2	89.0	N/A	
1995	90,046	1.7	28,922,775	0.5	91.4	72.4	88.0	N/A	
1996	99,072	10.0	32,689,797	13.0	93.4	75.7	90.4	N/A	
1997	105,347	6.3	33,222,230	1.6	90.3	68.8	86.4	N/A	
1998	109,365	3.8	34,249,837	3.1	90.3	67.3	85.8	N/A	
1999	120,294	10.0	38,638,433	12.8	92.1	68.6	88.0	N/A	
2000	124,270	3.3	40,414,468	4.6	92.5	71.9	89.1	N/A	
2001	126,610	1.9	39,142,115	(3.1)	88.9	63.8	84.7	$76.39	---
2002	126,787	0.1	38,872,894	(0.7)	88.8	60.2	84.0	76.69	0.4 %
2003	130,482	2.9	40,482,041	4.1	89.6	60.5	85.0	82.48	7.5
2004	131,503	0.8	42,526,755	5.1	92.0	68.7	88.6	89.78	8.9
2005	133,186	1.3	43,362,698	2.0	91.8	72.0	89.2	103.12	14.9
2006	132,605	(0.4)	43,415,540	0.1	93.2	65.2	89.7	119.66	16.0
2007	132,947	0.3	43,867,192	1.0	94.0	64.5	90.4	132.09	10.4
Year-to-date through November:									
2007	133,690	---	40,550,109	---	94.6 %	65.5 %	91.0 %	$133.76	---
2008	137,892	3.1 %	39,775,607	(1.9)	91.0	58.9	87.1	121.01	(9.5) %
Average Annual Comp. Change, 2004 - 2007:		0.4 %		1.0 %					13.7 %

Source: Las Vegas Convention and Visitors Authority of 13.7% due to the high quality of the new supply and removal of the lower-rated Stardust. However, as operators implemented strategies to compete for overnight guests to support gaming and other amenities, average daily room rates have declined 9.5% in the year-to-date period ending in November 2008. High-end operators, including Wynn Resorts and Las Vegas Sands Corp., have dramatically reduced average daily rates; thereby forcing lower quality properties to lower rates in order compete. Additionally, the number of convention attendees for 2008 through November was down 5.0% and the number of conventions/meetings held was down 5.2% according to the LVCVA. Further downward pressure on average daily rates has been caused by hotels replacing a decline in convention business with more leisure and casino customers taking advantage of low room rates and other specials since convention customers also typically pay more lucrative room rates.

Based on the year-to-date data presented in Table 2, it is evident that occupancy and average daily rate for Las Vegas properties have declined in 2008 due to economic conditions. However, since casino-resort operators are motivated to sustain occupancy because of the need to generate demand for the casino and other ancillary facilities, average daily rate has been affected more than occupancy levels.

Gaming Demand

In addition to reducing the number of people who come to Las Vegas, the recession is prompting the ones who do visit to spend less on their trips. Moreover, local gaming demand plays an important, albeit secondary, role in the Las Vegas market. 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, such as leisure, convention, and tour and travel segments; and, with less discretionary income and higher unemployment levels, lower gaming revenue from the local segment is expected.

The Las Vegas gaming market reached record highs annually from 2004 through 2007, due in part to the strong economy and opening of the Wynn Las Vegas, South Point, and Red Rock Station. Prior to 2008, there have been only two years since 1980 that the Las Vegas gaming market has contracted: 2001 and 2002. In 2001 and 2002, the gaming market contracted by 0.5% and 0.02%, respectively, which was attributable to the economic recession and the events of September 11. In 2002, the gaming market contracted by as the nation and region recovered from the economic recession. The historical gaming win, number of visitors, and gaming win per visitor for Clark County for 1980 to November 2008 are shown in Table 3 [page 5].

The Las Vegas gaming market over the past three decades has been a supply-driven market—i.e., "build it and they will come," where the significant continuous additions to supply have been readily absorbed. Recent performance of the Las Vegas market, however, is providing the first indication that the market has potentially reached a saturation point. The decline in gaming revenue for Clark County in the first 11 months of 2008 compared to 2007 of 9.0% is high due not only to the economic climate but also the recent multiple years of strong growth. The 5.4% decline in Clark County gaming win per visitors in the year-to-date period through November 2008 is indicative that the visitors that are coming are not gambling as much.

Four months in 2008 experienced significant declines relative to 2007: May (16.4%), July (15.0%), October (24.3%), and November (15.2%). Clark County gaming revenue by month for 2004 through 2008 is set forth in Chart 2 [page 6].

In October and November 2008, monthly gaming revenues fell below those achieved during the same months in 2004. It is estimated that the annual gaming revenue for Clark County in 2008 will be in the same range achieved in 2005; in the mid-$9 billion range.

Major Developments

Major recent developments in the Las Vegas market include the opening of Wynn Las Vegas' Encore in December 2008; the ongoing construction of

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Table 3 - Total Visitors, Revenue, and Win per Visitor (Clark County)

	Total Visitors		Total Revenue (Win)		Total Revenue (Win) per Visitor	
Year		% Change		% Change		% Change
1980	11,941,524	---	$1,617,194,799	---	$135	---
1981	11,820,788	(1.0) %	1,676,148,606	3.6 %	142	4.7 %
1982	11,633,728	(1.6)	1,751,421,394	4.5	151	6.2
1983	12,348,270	6.1	1,887,451,717	7.8	153	1.5
1984	12,843,433	4.0	2,008,155,460	6.4	156	2.3
1985	14,194,189	10.5	2,256,762,736	12.4	159	1.7
1986	15,196,284	7.1	2,431,237,168	7.7	160	0.6
1987	16,216,102	6.7	2,789,336,000	14.7	172	7.5
1988	17,199,808	6.1	3,136,901,000	12.5	182	6.0
1989	18,129,684	5.4	3,430,851,000	9.4	189	3.8
1990	20,954,420	15.6	3,871,097,504	12.8	185	(2.4)
1991	21,315,116	1.7	4,110,608,604	6.2	193	4.4
1992	21,886,865	2.7	4,230,751,572	2.9	193	0.2
1993	23,522,593	7.5	4,521,123,158	6.9	192	(0.6)
1994	28,214,362	19.9	5,431,474,872	20.1	193	0.2
1995	29,002,122	2.8	5,720,390,612	5.3	197	2.5
1996	29,636,361	2.2	5,783,610,126	1.1	195	(1.1)
1997	30,464,635	2.8	6,151,904,298	6.4	202	3.5
1998	30,605,128	0.5	6,347,696,977	3.2	207	2.7
1999	33,809,134	10.5	7,210,085,904	13.6	213	2.8
2000	35,849,691	6.0	7,673,134,286	6.4	214	0.4
2001	35,017,317	(2.3)	7,632,021,543	(0.5)	218	1.8
2002	35,071,504	0.2	7,630,272,759	(0.0)	218	(0.2)
2003	35,540,126	1.3	7,830,675,556	2.6	220	1.3
2004	37,388,781	5.2	8,711,243,614	11.2	233	5.7
2005	38,566,717	3.2	9,716,860,486	11.5	252	8.1
2006	38,914,889	0.9	10,630,387,000	9.4	273	8.4
2007	39,196,761	0.7	10,868,029,000	2.2	277	1.5
Average Annual Compounded Change, 1980 to 2007:		4.5 %		7.3 %		2.7 %
Average Annual Compounded Change, 1990 to 2007:		3.8		6.3		2.4
Year-to-date November:						
2007	36,120,930	---	$9,922,508,000	---	$275	---
2008	34,741,853	(3.8) %	9,025,194,000	(9.0) %	260	(5.4) %

Source: Nevada Gaming Control Board, Las Vegas Convention & Visitors Authority, HVS Consulting and Valuation

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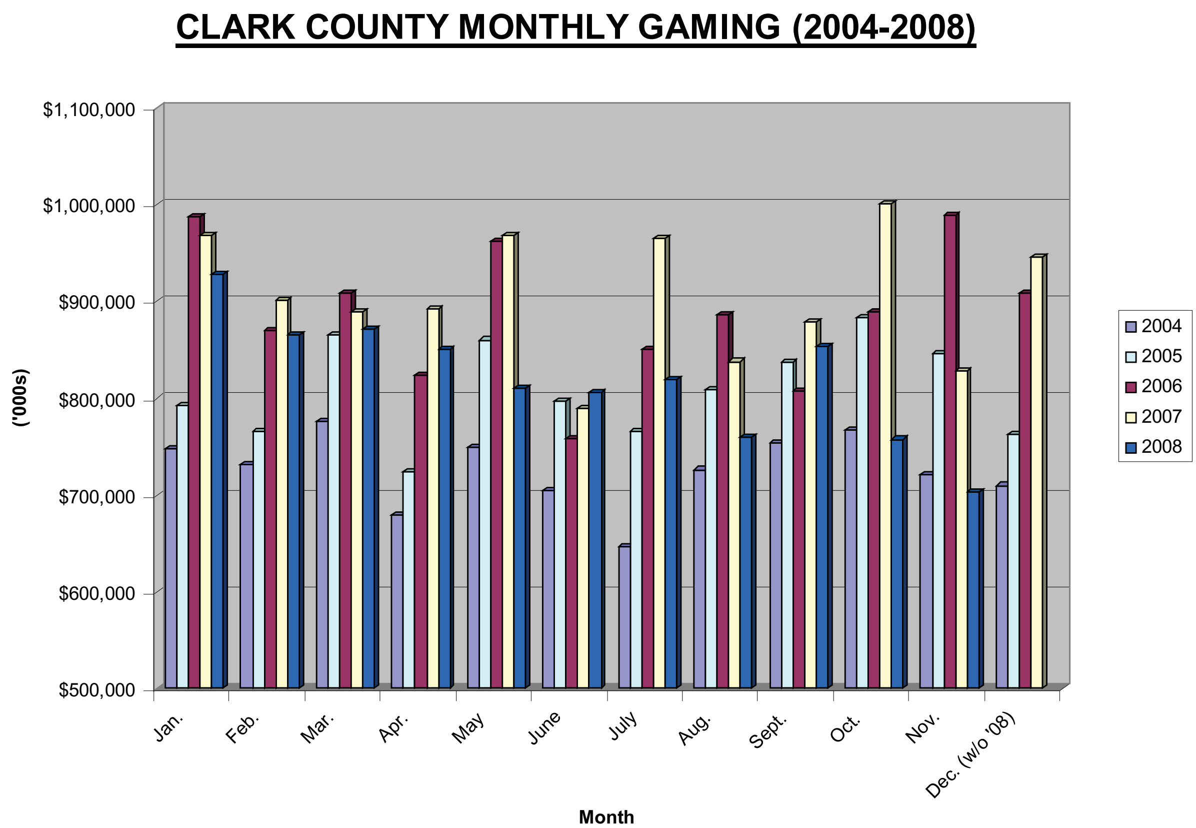
Chart 2 - Clark County Monthly Gaming Revenue (2004-2008)



CityCenter, the Fontainebleau Casino-Resort, and the Cosmopolitan; and the Hard Rock Hotel and Casino expansion, which all represent increases in gaming inventory, transient lodging supply, and/or function space, as well as factors contributing to the evolution of the Las Vegas area market.

- Encore, located on a ±20-acre site on the Strip immediately adjacent to the Wynn Las Vegas, opened in December 2008. Encore includes a 2,034 all-suite hotel tower fully integrated with the Wynn Las Vegas, as well as an approximately 72,000-square-foot casino, ±60,000 square feet of convention and meeting space, restaurants, a nightclub, swimming pools, a spa and salon, and retail outlets. The cost of the Encore development and capital improvements is estimated at approximately $2.3 billion.
- CityCenter is a 66-acre, mixed-use development project on the Las Vegas Strip between the Bellagio and the Monte Carlo casino-resorts owned equally by MGM-Mirage and by Infinity World Development Corp., a wholly owned subsidiary of Dubai World. The first phase of Project CityCenter reportedly will open in late 2009. Plans include multiple high-rise buildings with a contemporary urban design, with ARIA, a ±4,000-room resort with 150,000-square-foot casino, fine dining, and world-class entertainment, as the centerpiece. The Mandarin Oriental Hotel & Residences will feature 400 hotel rooms and 227 residential units and will be managed by the Mandarin Oriental Hotel Group. Veer Towers will contain 670 residential units in two towers surrounded by retail, restaurants, and entertainment. Vdara is a 1,495 hotel-condominium tower designed by Rafael Vinoly. Crystals retail and entertainment complex will offer approximately 76 outlets featuring high-end fashion, boutiques, dining,

and entertainment venues. In 2009 it was announced that the opening of the Harmon will be delayed to late 2010 and that the Harmon tower, originally planned for about 50 stories, will stop at about half that with the condominium component canceled. Construction issues were blamed on the delay. The move will save MGM Mirage roughly $200 million by deferring construction costs for a year. Coupled with other cost savings, MGM Mirage said it has shaved $600 million from CityCenter's $9.1 billion budget.

- Construction of the $2.9 billion Fontainebleau casino-resort has begun on a 24.5-acre site north of the Riviera on the Las Vegas Strip. The Fontainebleau reportedly will feature a 100,000-square-foot casino, 3,889 luxury hotel rooms and condominium-hotel units, food and beverage outlets, nightclubs, and 200,000 square feet of meeting and convention space. The project is slated to be completed by early 2010.
- Construction of the ±$3.5 billion, 3,000-room Cosmopolitan Resort & Casino has continued despite Deutsche Bank's foreclosure on the project that was begun by developer 3,700 Associates, LLC, headed by Ian Bruce Eichner. Reportedly, buyers have signed purchase contracts for more than 1,800, or more than 80 percent, of the property's nearly 2,200 condo-hotel units. The remaining 800 units were planned as hotel rooms. The original design called for a 70,000-square-foot casino, over 300,000 square feet of retail, and a 1,800-seat theater.
- Morgans Hotel Group Co. and DLJ Merchant Banking Partners are expanding and renovating the Hard Rock Hotel & Casino in Las Vegas. The expansion project will include the addition of approximately 875 guestrooms, including an all-suite 15-story tower with upgraded amenities, approximately 60,000 square feet of meeting and convention space, and approximately 30,000 square feet of casino space. In addition, the project includes the expansion of the Hard Rock's pool, new food and beverage outlets, a new and larger live-entertainment venue, 30,000 square feet of new retail space, and a new spa and health club. As part of the project, the Hard Rock's existing suites and common areas will be renovated. The project is expected to be completed by late 2009.
- Other gaming projects recently completed, or near completion, in the market include Aliante Station, which opened in North Las Vegas in November 2008, and the M Resort, which is planned to open in March 2009 in Henderson.
- A joint venture led by a holding company that includes the AFI Group is reportedly applying for use permits to build the world's largest hotel (6,745 rooms) in four high-rise towers on 60 acres along Harmon Avenue west of the Hard Rock Hotel. The resort reportedly will include a casino and a retail complex. No price on the project was publicly available.

While these developments are expected to drive additional visitation, it is likely that the market will not absorb new lodging and gaming inventory as rapidly as it has historically. Developers of other projects have recognized the potential for oversupply in the market and, combined with the tightening credit requirements, softening interest in residential properties, and declining gaming and hotel demand as a result of the current credit crisis, the following projects have been postponed or cancelled, most notably Boyd Gaming's Echelon project.

- Echelon is planned to be a multifaceted, world-class resort complex located on a 63-acre site on the Las Vegas Strip. The development is expected to be among the most significant projects in Las Vegas' ongoing evolution. The development is anticipated to be a significant leader in Las Vegas' key growth centers of casino gaming and luxury hospitality, including world-class dining and nightlife experiences, shopping, meetings and conventions, and entertainment. Hotels planned for the complex initially included the 3,300-room resort hotel, as well as Shangri-La, Delano, and Mondrian hotels, with a total guestroom inventory of approximately 5,000. Echelon's public areas are expected to contain

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a 140,000-square-foot casino, 25 restaurants and bars, and landscaped pool and garden areas. The Las Vegas ExpoCenter at Echelon Place is planned to include 650,000 square feet of exhibition and pre-function space and 175,000 square feet of meeting and conference space. Combined with the meeting space within Echelon Resort, the total meeting and exhibition space at Echelon Place is planned to exceed one million square feet, highlighted by over 200 meeting rooms.

On August 1, 2008, Boyd Gaming announced that, due to the difficult environment in the capital markets, as well as weak economic conditions, the Echelon project on the Las Vegas Strip had been delayed. Boyd Gaming reportedly has expended over $600 million, not including land, on the Echelon project. No definitive timetable for resumption of construction has been announced. However, given the project's favorable location and amount expended to date, it is anticipated that the project will resume once market conditions improve.

- The 34-acre New Frontier Hotel and Casino on the Las Vegas Strip was imploded in November 2007 to make way for the construction of a $5.0+ billion replica of the famed New York Plaza Hotel. The property is being developed by EL AD IDB Las Vegas LLC, which is wholly owned by partnership between EL AD Properties Las Vegas LLC and IDB Group USA Investments Inc. The Plaza Las Vegas reportedly would feature over 4,000 hotel rooms, 2,000 resort condominium units, and ±150,000 square feet of casino, restaurant, retail and convention space. The project has been delayed and is expected to open in 2013.
- Stockbridge Real Estate Funds of San Francisco announced the remodeling plans for the Sahara, which will include a new high-rise hotel tower and the demolition of the property's older mid-rise tower. Los Angeles-based SBE Entertainment Group, the operating partner, and Stockbridge Real Estate Funds of San Francisco purchased the Sahara in 2007. The plans approved by Clark County include a new 520-foot hotel tower with 1,000 rooms, the renovation of the existing two high-rise hotel towers, and the removal of the 200-room mid-rise tower. Upon completion, the Sahara will have 2,506 hotel rooms. In addition, the Sahara will be reconfigured to contain 90,000 square feet of casino space, 56,900 square feet of retail space, 78,900 square feet of restaurant space, a 19,000-square-foot entertainment venue, 26,600 square feet of nightclub space, 32,600 square feet of meeting and convention space, and a 22,600-square-foot spa and fitness center. No timetable for the project has been announced.
- The 665-room Octavius Tower, the sixth hotel tower at Caesar's Palace, was topped off in October 2008 and was scheduled to open in 2009. However, on January 12, 2009, Harrah's Entertainment confirmed that completion of the Octavius Tower had been suspended until a period of stronger demand. Other parts of the company's $1 billion expansion, including 110,000 square feet of additional meeting space, are still scheduled for completion in 2009.

Projects cancelled or put on hold indefinitely in 2008 include the Crown Las Vegas, a joint venture between MGM Mirage and Kerzner International Holdings Limited, and the St. Regis Residences, which was planned for development by Las Vegas Sands.

Conclusion

The risk of further decline in local, national, and worldwide economic conditions is greatly concerning operators in the Las Vegas market. Visitation to Las Vegas and the amount spent per visitor are in decline, resulting in deteriorating revenue and net income levels for Las Vegas casino hotels. While this is perceived as a cyclical downturn, the duration and magnitude of the downturn are uncertain at this time. Significant increases in competition from other gaming markets, both internationally and in the United States, may also have a negative impact upon the future performance of the Las Vegas market.

Overall, the Las Vegas market is expected to

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experience slowed economic growth in the short term as a result of the downturn in the national and worldwide economies. However, the Las Vegas market has historically weathered periods of economic decline and downturns in visitation well. While visitation may decline in 2009 and into 2010, a rebound is expected once the national and world economies recover. The market is expected to rebound when tourism demand from local, national, and international sources increase as a result of cyclical market forces and the inducement caused by the completion of expansions and development of product offerings. Las Vegas is a unique, iconic gaming and entertainment mecca and, with an estimated local population of 1.8 million people and well over 35 million tourists visiting the metropolitan Las Vegas area annually, the amount of existing and potential gaming activity is significant. Given its critical mass and billions of dollars in invested capital, Las Vegas will continue to be an eminent domestic and international gaming destination.

The current financial crisis has curtailed lending on major development projects. The investment banking firms that were responsible for financing the recently constructed casino hotels in Las Vegas are in a state of transition, and it is uncertain what the future source of debt financing for large-scale casino hotel projects will be. Even major gaming companies such as MGM-Mirage have resorted to sales of assets to improve liquidity positions due to declining cash flow. One source of cash infusion into the market may be cash-rich gaming companies such as Penn National, which received roundly $1.5 billion as a result of the termination agreement with Fortress Investment Group LLC and Centerbridge Partners, L.P., or other investment groups seeking bargains during the down market.

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