

Detroit rolls dice by relying on casino cash

Sun, Jun 8 2014

By Tim Reid and [Michael Erman](#)

DETROIT/NEW YORK (Reuters) - Detroit's reliance on casino cash to help fund a recovery from the city's historic bankruptcy is a high-risk bet on what is an increasingly shaky source of income.

A trial to approve Detroit's plan to exit its \$18 billion bankruptcy, the largest municipal crash in U.S. history, begins in late July. Flawed revenue projections may undermine its feasibility, creating a key legal hurdle to win approval by the court. On a practical level, a revenue shortfall could knock the city down just as it is getting back on its feet.

Detroit Emergency Manager Kevyn Orr projects that wagering tax revenue from three local casinos, the city's third largest source of cash, will remain essentially steady as far ahead as 2023.

Orr has described the gambling taxes as Detroit's most stable source of money. But casino revenue has declined of late in Detroit itself and in recent years traditional gambling hubs like Nevada and New Jersey as well as relative newcomers to the wagering scene, such as neighboring Ohio, have seen swoons.

"Projecting casino revenue is notoriously difficult," Moody's Investors Service casino analyst Keith Foley said. "But nobody is saying it is going to get better."

For instance, casino revenue from Atlantic City has roughly halved since 2007, a drop no one saw coming, Foley said. Total U.S. casino revenue in 2012 was still just shy of a 10-year peak of \$37.5 billion set in 2007, according to the American Gaming Association.

A litany of factors stack up against Orr's forecast, industry analysts and experts say: younger people show little interest in gambling, the casino market is saturated, and thousands of local residents are likely to see their wages drop due to the bankruptcy plan.

Bill Nowling, a spokesman for Orr, says the casino tax projection is conservative and was calculated by Detroit's financial restructuring advisors, Ernst & Young. He said the calculations were also based on anticipated Michigan unemployment rates "continuing to improve and inflation to hold at or below 1 percent annually."

He declined to elaborate on projections but said if they were too high, Detroit "will live within its means and will match spending with available revenue."

The casino revenue has already been the subject of legal wrangling in the bankruptcy. In April, the bankruptcy judge approved a deal brokered by Orr that kept the casino revenue from being diverted to two creditor banks.

THE RISK OF A DROP

In fiscal year 2013, casino taxes brought in \$174.6 million, down 3.7 percent from \$181.4 million the year before, according to Orr's latest plan of adjustment filed in May. That was nearly 17 percent of Detroit's general fund revenues, with only income taxes and state funds larger revenue sources.

Orr's plan predicts it will continue to drop to just over \$168 million in 2015, then recover to its 2012 level by 2023, at a growth rate of 1 percent a year from 2016 until 2023.

But just a 1 percent annual downturn in wagering taxes after 2016 would lead to a more than \$25 million shortfall in 2023 alone, according to calculations by Reuters.

Overall, revenue at the three casinos fell 4.75 percent in 2013. The decline has continued so far this year, with revenue over the first four months falling more than 6 percent from a year earlier.

"Obviously they are going to have to justify this projection at trial," said Richard Larkin, director of credit analysis at investment bank HJ Sims. "Casino revenue is not a traditional, long-term revenue source."

A flaw in projecting casino revenue "could signal far deeper problems with city's plan of adjustment and the city's intended plans for recovery," said Peter Hammer, a law professor at Detroit's Wayne State University.

"It decreases substantially the confidence you have about the viability of the rest of the plan, which involves much more complicated issues," Hammer said.

Moody's Foley has a similar concern about the casinos: "What if Detroit has another 5 percent decline next year? Then their budget is already way off track."



After all, Detroit is not alone in seeing a fall off in casino revenue. It is down in Illinois, Indiana, Iowa, Nevada, Pennsylvania, Missouri, Connecticut, Atlantic City and Ohio in the past two years, according to figures from each state.

TEMPORARY OR LONG-TERM DECLINE?

Analysts and backers of Orr's projections say there are factors that might mitigate a slide in Detroit's casino revenue, compared to other areas. State law allows only three gambling houses in the city, a cushion against more competition. The city is the most convenient gambling center for southeast Michigan, northeastern Indiana and northwest Ohio.

Jennifer Kulczycki, a spokeswoman for the company that owns one of the city's casinos, Greektown, said that while revenue had softened, "we are optimistic for things to return to previous levels - and then some. The Detroit market is 14 years old and it has been very resistant."

A central issue is whether these declines are temporary or permanent.

In an April report, Moody's Foley warned that Detroit's bankruptcy threatens a reduction in gambling spending because city employees face lower pensions and retiree health benefits under Orr's restructuring plan. The city is Detroit's second biggest employer, according to Crain's Detroit Business.

Demographics are also a worry, said Alex Calderone, a business turnaround specialist based in Michigan, who was part of the team that took the city's Greektown Casino-Hotel through bankruptcy between 2008 and 2010. Greektown is up and running under a new owner - Dan Gilbert, the founder and CEO of Quicken Loans, who is investing heavily in downtown Detroit.

Standing in the casino, surrounded by the cacophony of slot machines and clouds of cigarette smoke, Calderone asked: "Where are the young people?" There is no replacement for the predominately older age group who gamble, he said.

"Young people have little inclination to play slot machines," according to a recent analysis by Deutsche Bank. It cited research by the Meczka consulting group, which said only 18 percent of people aged between 21 and 35 visit casinos.

IN AN URBAN DESERT

Experts also look to Las Vegas as a leading indicator in gambling behavior. According to the Center for Business and Economic Research at the University of Nevada, more people now visit the Vegas strip to eat and go night clubbing than gamble.

But Detroit is not Vegas. Casino-hotels on the Vegas strip such as Caesar's Palace and Wynn Las Vegas have spectacular nightly shows, and high-end bars, restaurants and shops. Moreover, Detroit's casino tax is based on gambling revenue alone.

While Detroit's biggest casino, MGM Grand Detroit, part of MGM Resorts International(MGM.N: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)), would not look out of place among the glass and marble casinos of the Vegas strip, it and the nearby MotorCity sit in a virtual urban desert. Their surroundings are bleak - a far cry from glitzy - and perpetually warm - Las Vegas.

Last year revenues fell 6.3 percent at the MGM and 1.2 percent at MotorCity, and have continued to drop this year. Greektown's revenue fell more: from \$352.1 million to \$328.3 million, or 6.8 percent.

In contrast to its larger two rivals, Greektown is in need of a makeover. Its carpets are old, its facilities drab.

But plans for a full face lift have been scaled back. According to a February filing with the Securities and Exchange Commission, Gilbert's company that owns Greektown, Athens Acquisitions LLC, said a planned \$150 million renovation had been cut back to a \$25 million to \$50 million refurbishment.

"In a casino that's basically just changing the carpet," said Ken Adams, a gaming consultant.

(Reporting by Tim Reid; Editing by Dan Burns and [Peter Henderson](#))
