

The Las Vegas Metamorphosis – From Gaming to Entertainment Destination

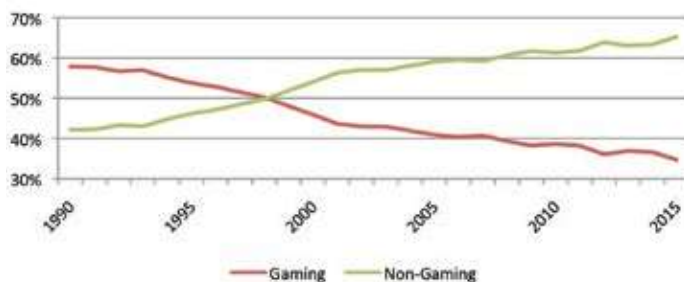


Stewart Rubin
Senior Director
New York Life Real Estate Investors

Las Vegas hosted a record number of visitors in 2015 as tourism increased 2.5% over 2014 to 42.3 million tourists. Visitation now stands 8.0% higher than its 2007 prerecession peak, while gaming revenue is down 11% during the same time period. What is going on? Can gaming decline and Las Vegas still thrive? The answer is that Las Vegas has undergone a metamorphosis becoming a more diverse entertainment destination and gaming is no longer the primary revenue generator. During the same time period, total non-gaming revenue was up 15.5% resulting in an overall revenue increase of 4.8%.

The transformation of Las Vegas from a primarily gaming zone to an entertainment destination became apparent in 1999 when non-gaming revenue surpassed gaming revenue for the first time. This trend has accelerated since then as non-gaming revenue reached 65.3% of total revenue in 2015, up from 51.3% in 1999 and 42% in 1990.

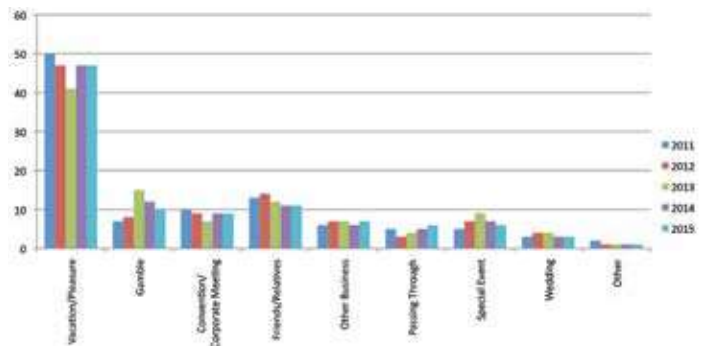
Table 1
Share of Revenues



Source: Nevada Gaming Control Board

Visitors once travelled to Las Vegas to gamble and were treated to ancillary entertainment, maybe a show and food – which was not so great. Now Las Vegas is attracting visitors who are drawn primarily for entertainment. According to the Las Vegas Convention and Visitors Authority (LVCVA), almost 50% of visitors to Las Vegas report that their primary reason for visiting Las Vegas was vacation/pleasure compared to approximately 10% who cited gambling.

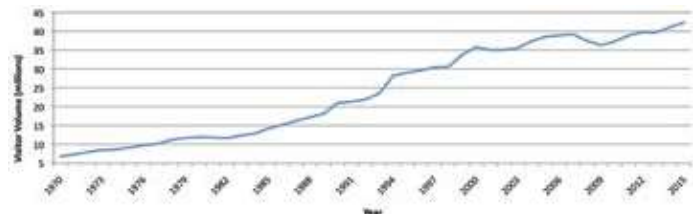
Table 2
Primary Reason for Visiting Las Vegas



Source: GLS Research Prepared for Las Vegas Convention and Visitors Authority

Gaming revenue is now at its lowest level since 2005; conversely, non-gaming revenue is at its highest level ever. The non-gaming entertainment category includes rooms, restaurants, night clubs/day clubs, and shows. In addition there are extra-resort entertainment venues that are proving to be tourist draws including concerts/live music, dance festivals, and shopping. Professional sports may prove to be an additional draw going forward. This transformation has resulted in a 25% increase in visitation since the 1999 crossover point and a 10% increase since 2005.

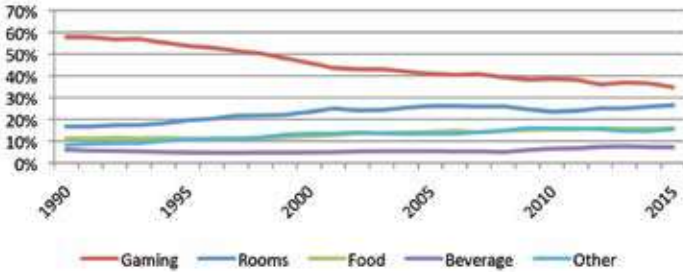
Table 3
Historical Visitor Volume



Source: Las Vegas Convention and Visitors Authority (LVCVA)

The following tables illustrate the divergence of revenues between gaming and individual non-gaming revenue categories since 1990.

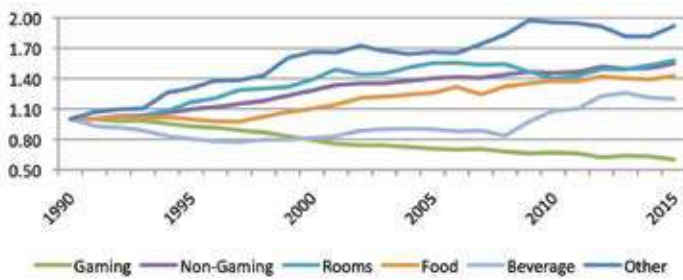
Table 4A
Share of Revenues



Source: Nevada Gaming Control Board

Table 4B presents the same data in the form of an index.

Table 4B
Share of Revenues Indexed to 1990



Source: Nevada Gaming Control Board

Gaming

As the national economy climbed out of recession over the past five years, Las Vegas gaming revenues increased 13%. However, over the past ten years, gaming revenue remained stagnant with only a 0.2% increase. The average gambling spend per visitor has decreased 11% from \$652 in 2006 to \$579 in 2015. Gaming revenues are down 4% from 2014 to 2015. From 2010 to 2014, Las Vegas casinos benefitted from large-volume international gamblers replacing smaller domestic gamblers¹.

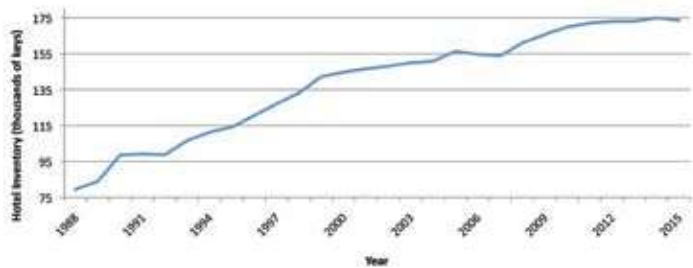
Non-Gaming Categories

Activity diversification has manifested itself in different ways in the following categories.

Lodging/Rooms

The impact of Las Vegas revenue source diversification has been positive for the lodging sector. The expansion of alternative entertainment options has created more reasons to visit Las Vegas and to patronize hotels and visitation has increased 25% since the 1999 crossover point according to LVCVA. This has also resulted in more rooms being constructed. Since 1999, Las Vegas' supply of hotel rooms has increased by 23% to approximately 175,000 as of Q3 2016 according to CoStar.

Table 5
Historical Hotel Inventory (Annual Average)

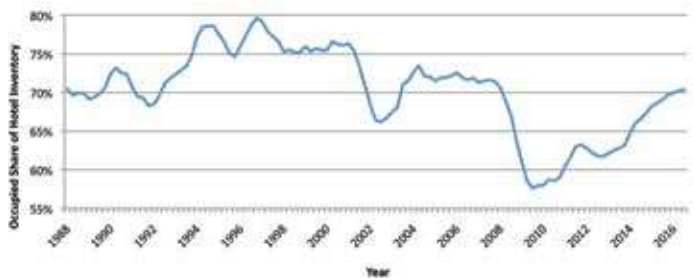


Source: CoStar

Room revenue, occupancy and the amount spent per visitor on lodging are all up. Over the past five years, as the nation's economy rose out of recession, room revenue increased 42% at Las Vegas resorts. Resort room revenue is up 20.2% over the past ten years and up 4.4% from 2014 to 2015².

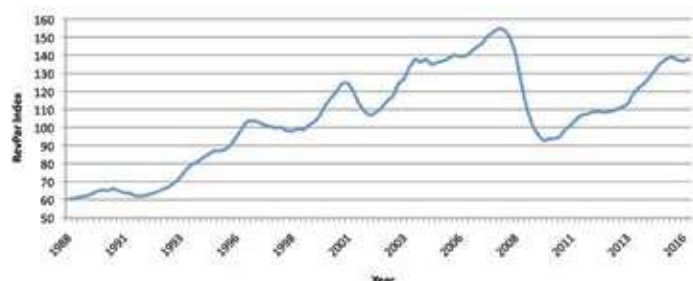
According to CoStar, the overall Las Vegas metro hotel market occupancy rate of 70.4% is at its highest level since its most recent prerecession peak in the fourth quarter of 2007. It has recovered considerably from its nadir of 57.6% in the third quarter of 2009. Its four month moving average RevPAR of \$137.85 is close to a seven year high.

Table 6
Las Vegas Hotel Occupancy Rate (Four-Quarter Moving Average)



Source: CoStar

Table 7
Las Vegas Hotel Index of Revenue Per Available Hotel Room (RevPAR) (Four-Quarter Moving Average)



Source: CoStar

As more visitors travel to Las Vegas for non-gaming entertainment, demand has risen for gambling free and smoke free hotels including Mandarin Oriental Hotel, Vdara Hotel, Four Seasons, Signature at MGM Grand, Trump Hotel and the Marriott Vacation Club.

Restaurants

Las Vegas food options are no longer primarily focused on buffets; alternatives now include a wide range of high-end eateries including celebrity chef restaurants with international cachet. The range includes Restaurant Guy Savoy, a French restaurant situated in Caesar's Palace Hotel, Bar Masa a Japanese restaurant in the Aria Hotel and Carnevino, a steakhouse owned by Chef Mario Batali and his business partner Joe Bastianich in the Palazzo Hotel. Chef/owner Costas Spiliadis owner of restaurants in Montreal, New York and Athens, operates Estiatorio Milos in the Cosmopolitan Hotel. Las Vegas is also host to the only Joël Robuchon eatery in the world run by the eponymous chef and situated in the MGM Grand Hotel. Other high end eating adventures include: Le Cirque and Picasso, where expensive art work can be experienced together with quality food both situated in the Bellagio Hotel. Therefore, it should come as no surprise that food revenue at resorts has increased 34% since 2005, 31% in the past five years, and 3.75% in 2015 year over year. The average food and drink spend per visitor has increased 12% from \$261 in 2006 to \$292 in 2015³.

Nightclubs and Dayclubs

The fastest growing revenue center of the past decade was nightclubs/dayclubs. According to the Nightclub & Bar Media Group, Las Vegas secured seven of the top 10 spots (including the top four) on its annual list of top grossing bars and nightclubs in the United States in 2015.

XS, at the Wynn Las Vegas & Encore Resort occupied the top spot for the third year in a row. Hakkasan, a very large club with several venues in Las Vegas owned by its parent company and famous for its renowned guest DJs secured the number two spot while Marquee situated in the Cosmopolitan Hotel came in third followed by TAO located in the Grand Canal Shops at the Venetian Hotel. The sixth, ninth and tenth highest grossing are the Las Vegas night spots of Surrender (also at the Wynn), Hyde Bellagio (situated behind the Bellagio Fountains), and LAVO Las Vegas (situated in the Grand Canal Shops).

Other Hakkasan Group clubs include Omnia with a 4,500 person capacity which opened in 2015 and Jewel with a 2,000 person capacity. Sayers Club which boasts the most live music of any other club in Las Vegas and Foxtail at the SLS hotel. Other Las Vegas nightclubs that are big draws include Drai's After Hours and Light — created by Cirque du Soleil.

Younger visitors have been a catalyst sparking demand. The average age of visitors as of 2015 was 47.7 compared to 49.0 in 2011 and 50.0 in 2009. The younger demographic is more attracted to Las Vegas's entertainment offerings and less likely to gamble.

Nightclubs are the most popular, but day clubs, where DJs play at hotel pools is a newer source of growth. Beverage revenue, a proxy for night and day club revenue, at Las Vegas resorts is up 57% over the past ten years, 40% over the past five years and 0.3% from 2014 to 2015⁵.

Shows

Las Vegas is home to many successful shows catering to a variety of tastes. Top grossing shows include Cirque du Soleil shows, Terry Fator (an illusionist), Le Rêve, and "Jersey Boys," Penn & Teller at Rio (a magic show), "Smokey Robinson presents Human Nature: The Motown Show" and Blue Man Group at Luxor are other popular acts.

The average show spend per visitor had increased 21% from \$51 in 2006 to \$62 in 2015. Between 2011 and 2015 spending per visitor increased by 30% from \$48 to \$62. The proportion of people who attended any shows during their stay in Las Vegas has ranged between 60% and 72% over the past five years and was 61% in 2015, however, among those who attended shows, the proportion who attended big-name headliner performances increased from 17% in 2011 to 26% in 2015. Shows are included in the "other" revenue category of Las Vegas resorts which is up 7.1% from 2014 to 2015. It is up 24% over the past five years and up 37% over the past ten years⁶.

Concerts/Live Music

Historically Las Vegas was a music venue where older entertainers past their prime went to finish out their careers. Music used to be a way to attract gamblers to Las Vegas, but has evolved to be an independent draw.

According to Pollstar, 2015 was a record year for the North American concert business with Top 100 Tours earning \$3.12 billion, up 14% over 2014. Las Vegas is now claiming its share. The number and size of venues that can accommodate concerts has expanded and is now approaching the capacity of much larger cities.

The largest live music venue in Las Vegas is the newly built 20,000-seat T-Mobile Arena opened by MGM Resorts International (MGM) and Anschutz Entertainment Group (AEG). That was the first new venue of its size to open in the city in two decades. The second largest is the Thomas & Mack Center with a 19,522 seat capacity. Madison Square Garden Co., Live Nation, and Las Vegas Sands Corp. plan to open a 17,500-seat concert venue on the Las Vegas Strip. This would become the third largest concert venue in Las Vegas. With the addition of this new arena, Las Vegas will have five arenas each with over 12,000 seats — all an appropriate size for concerts. Older existing arenas include the 16,800-seat MGM Grand Garden Arena inside MGM's casino and the 12,000-seat Mandalay Bay Events Center. Music stars that have played in Las Vegas over the past two years include Future, J.Lo, Pitbull, Bruno Mars, Guns N' Roses and Drake.

Las Vegas is also host to popular dance festivals such as the Electric Daisy Carnival which experienced its sixth year. Other dance festivals include Rock in Rio USA which has been in Las Vegas since its inaugural 2015 US season.

Artist residencies are acts, in which artists play in one venue exclusively instead of touring, have long been a Las Vegas mainstay. Historically it has attracted mature legacy acts such as Elvis Presley, Wayne Newton, Liberace and Sammy Davis Jr. Today's residencies, however, are current acts such as Jennifer Lopez, Drai, and Future. The turning point was 2003 when Celine Dion started her residency in the 4,000 seat Caesar's Palace Coliseum.

Population growth is another factor fostering local demand. According to the US Census, the population of Las Vegas has increased at an annual growth rate of 1.9% over the past ten years compared to 0.8% for the US. The forecast growth rate is 2.6% compared to 0.8% for the US. In addition aspiring artists can more easily afford to live in Las Vegas compared to Los Angeles and the same is true of older rockers past their prime as well.

Sports

On June 22, 2016, the National Hockey League (NHL) announced that Las Vegas would be receiving an expansion franchise. The team will begin playing in the 2017/2018 season at the newly opened 20,000 seat T-Mobile Arena on the Strip's south side. This would be the first of the four major professional sports leagues to situate a team in Las Vegas.

On October 17, 2016 Nevada Governor Brian Sandoval signed two bills that approved funding toward helping finance a proposed \$1.9 billion, 65,000-seat stadium in Las Vegas. The stadium would be the home of the National Football League's (NFL) Oakland Raiders. There are still significant hurdles to the Raiders relocation, including convincing 24 of the league's 36 owners to approve the move, but it is nevertheless, a step in the direction of expanding professional sports in Las Vegas and an indication that the city and state are supporting it.

The Las Vegas Sands/MSG, a 17,500-seat arena, is expected to be built on the north side of the Strip behind the Venetian's Convention Center. This venue may be the future home of the University of Nevada, Las Vegas NCAA football team.

Retail/Shopping

Retail centers based in the Strip are unique in that they cater to a tourist clientele yet attract a strong local customer base. Las Vegas ranked third in the United States behind only New York and Chicago in terms of its luxury retail presence⁷. The Las Vegas Strip has several high-end malls and retail centers. They include the 262,000 square foot Shops at Crystals Run built in 2009 and the 806,000 square foot Grand Canal Shops built in 1999 and renovated in 2007, and the 650,000 square foot Forum Shops at Caesars built in 1992 and renovated in 2004. The Forum Shops

at Caesars ranks as one of the top five shopping centers in terms of sales per square foot in the United States⁸. All three are very high end, high grossing retail malls situated at Las Vegas Boulevard resorts.

Wynn Plaza, which is scheduled to open in the fourth quarter of 2017, will be a 75,000 square foot luxury retail center at the Wynn Las Vegas. This addition will bring the total retail square footage at Wynn Las Vegas to more than 173,500 square feet. Wynn Las Vegas and the Encore currently have 25 luxury retailers such as Hermes, Dior, Chanel, and Piaget. It is important to note that this 75,000 square foot addition will be open to the street. This represents a departure from the traditional business strategy of necessitating that retail customers enter the resort and pass by gambling halls in order to get to retail and entertainment attractions. It further emphasizes the diversification of resorts away from their historic gaming focus.

Retail on the Strip is not limited to the high end, as visitors of more modest means can experience Las Vegas shopping at more moderately priced retail establishments. Fashion Show Mall is also located on the Strip but is a traditional mall catering to a diverse economic base. Built in 1981 and renovated in 2003, it includes 1,890,000 square feet and is anchored by Macy's, Dillard's, Saks Fifth Avenue, and Niemen Marcus.

Miracle Mile Shops at Planet Hollywood Resort & Casino was built in 2000, renovated in 2016 and includes 500,000 square feet of retail and entertainment space on the Las Vegas Strip featuring 170 specialty stores, over 20 restaurants and three live entertainment venues. It includes more affordable fashion choices such as H&M, GUESS by Marciano, Urban Outfitters, and True Religion Brand Jeans. The Showcase Mall entertainment and retail complex is located on the south end of Las Vegas Boulevard and includes Ross Dress for Less and a 20,000 square foot Adidas store. Further north on Las Vegas Boulevard is the Somerset Shopping Center also anchored by Ross Dress for Less.

Las Vegas revenue source diversification has coincided with a significant increase in retail inventory. Las Vegas retail inventory has grown by 75% since 1999 and by 27% since 2005 compared to 28% and 12% for the nation⁹.

The non-gaming tourist is by definition open to other ways to spend money in Las Vegas including shopping. In addition, the expansion of alternative entertainment options has created more reasons to visit Las Vegas and to do shopping while there. Conversely, shopping must compete with more numerous and varied entertainment alternatives for tourist dollars. According to Cushman and Wakefield the Strip retail submarket had a vacancy rate of 4.2% during trailing twelve months year ending Q3 2016. The aforementioned submarket includes Forum Shops, Canal Shops, Miracle Mile Shops, Fashion Show Mall, and Showcase Mall all of which have exhibited a recent 100% occupancy snapshot.

According to LVCVA, visitor retail spending was the third largest non-gaming expenditure after accommodations and food and beverage, at an average of approximately \$123 per person as of year-end 2015. The average retail spend per visitor had increased 6% from \$141 in 2006 to \$150 in 2014 before dropping to \$123 in 2015. When considering the increase in Las Vegas visitation over the past several years, total retail revenues are up 3.6% since 2011. Between 2011 and 2014 the amount spent per visitor increased by 16% from \$129 to \$150.

The \$123 per person figure marks a five-year low for the shopping category, while hotels, food and drinks, transportation, shows and sightseeing all hit a five-year high in 2015. This is likely the result of the strengthened US dollar and the consequential decline in international tourism. The proportion of foreign visitors declined from 19% in 2014 to 16% in 2015 according to LVCVA. International visitors tend to shop more on their trips to Las Vegas than domestic visitors. Another explanation is that this may be a data anomaly and that higher numbers will become apparent at the next survey.

The above notwithstanding, as the visitor base of Las Vegas diversified away from gaming, it is welcoming a guest that is open to new/other experiences such as shopping. When international travel rebounds it should also bring an increase in retail revenue.

Other Commercial Real Estate

Since 1999 inventory is up across all sectors, however, rent and occupancy performance has varied. On a metro wide basis, retail is overbuilt. Since 1999 retail inventory is up 75%, rent is down 12% and occupancy has fallen to 91% from 96%. Retail has not recovered from the most recent recession and rents are now 37% lower than at their height in 2007. However, Las Vegas Boulevard Strip retail, which is the most directly impacted by the higher visitation, maintains a low 4.2% vacancy rate¹⁰ with many of the centers observed to be at 100% occupancy. Strip rent levels are the highest in Las Vegas¹¹.

Office space is also overbuilt. Since 1999 office inventory is up 81%, rent is down 18% and occupancy has fallen to 85% from 94%. As of Q3 2016, rents are 26% below their peak in 2008. Industrial rent levels have also not recovered back to their pre recession levels.

According to the Case Shiller index, Las Vegas housing prices are still 35% below their peak in 2006 while the national index has fully recovered. The Las Vegas housing bust resulted in a lower home ownership rate which when considered together with population growth spawned greater demand for multifamily. Since 2007 Multifamily inventory is up 12%, rent is up 5% and occupancy has increased to 94% from 91.5%.

Conclusion

Las Vegas revenue source diversification has had a positive impact on the metro area economy and allowed it to thrive when other gaming centric markets have stumbled. Visitation is up significantly and population has grown faster than the nation.

The two commercial real estate sectors most positively impacted are lodging and Las Vegas Strip retail. The multifamily sector benefitted from the housing bust as well as population growth. Other sectors including office, metro-wide retail and industrial have not recovered to their prerecession rent levels.

Revenue source diversity has added to the stability of the metro area economy; nevertheless, we believe Las Vegas remains a market exposed to overbuilding and volatility for most property types.

DISCLAIMER

The information presented herein represents the view of the author as of the date of publication and is for informational purposes only. The information herein was obtained from various sources we believe to be reliable but Real Estate Investors makes no representation or warranty as to the accuracy or completeness of any third party information or data. The charts and graphs provided herein are for illustrative purposes only to assist readers in understanding economic trends and market conditions

1 Data for this paragraph is from Nevada Gaming Control Board (NGCB) and Las Vegas Convention and Visitors Authority (LVCVA)

2 NGCB

3 Spend per visitor data is based on the LVCVA survey conducted by GLS Research, while resort revenue is based on actual data from the NGCB. Since these two metrics are based on two different methods they may not match.

4 GLS Research Prepared for Las Vegas Convention and Visitors Authority

5 NGCB

6 Data in this paragraph from LVCVA and NGCB

7 "The New World of Retail-2015, Why the USA remains the destination of choice for luxury and international retail", Jones Lang LaSalle, December, 2014

8 IBID

9 Except where otherwise noted, data in this section is from CoStar

10 Cushman and Wakefield

11 IBID ■