TFA Monthly Newsletter

October 2012

Headline News:

9/26/12: Odawa tribe planning $26 million casino in Michigan (www.gamingtoday.com)

9/19/12: Arbitration Panel set for NY, Senecas over casinos (www.finance.yahoo.com)

9/12/12: Fitch Revises Quechan Rating Outlook to Positive; Affirms IDR at 'CCC'; Gaming Revenue Bonds at 'B-' (www.marketwatch.com)

9/12/12: Appeals court to allow tribe to take casino land near Glendale into trust (www.azcentral.com)

9/10/12: Legends Casino builds new day care center (www.kndo.com)

9/7/12: Santa Ysabel Casino Chapter 11 Bankruptcy Case Dismissed (nativeamericanlawfocus.com)

The Cash Flow Tug of War

by Kristi Jackson

There is a constant tension – what to do with extra free cash flow from casino operations? In any business, other than just building up cash, the owners can choose to reinvest, pay down debt or make a dividend. In the context of a tribal gaming business, the dividend isn't typically all discretionary – it is used to fund essential government services and programs. These services are critical to the stability of a Tribe and have to always be a central focus in the cash flow tug of war.

We know of many tribal gaming properties around the country where when revenues fell over the past 4 years, tough decisions were made – they spent less on maintenance in order to preserve a distribution stream to the tribal government. This is a tactic that can only work for so long… at some point, a lack of maintenance will lead to customers noticing and losing interest in the property. Who wants to walk around on worn or ragged carpet? What if air conditioning or ventilation systems break down – what sort of customer would want to sit in a hot and stuffy building? We know of one property where maintenance crews literally need to walk on the roof with hoses several times each day to keep the A/C systems from overheating due to a critical lack of reinvestment in replacing them over time. This is clearly not sustainable (or safe…).

The same analogy holds for paying down debt versus making a distribution to fund the government. At times, having an interest-only loan option seems attractive. When you are building something, for example, you really don't want to be simultaneously repaying debt. It makes sense to pay just interest during construction as you

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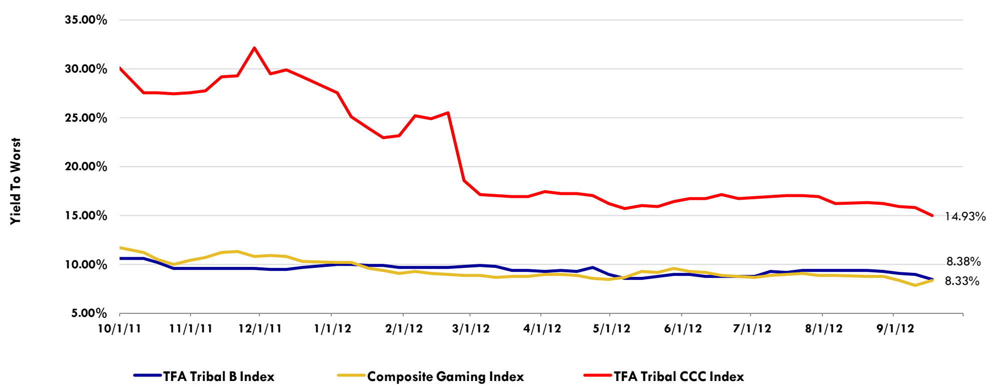
TFA Index Chart: A Comparison of HY Bond Interest Rates



Source: Wall Street High Yield Research

Notes: Yield to Worst represents the current average interest rate on bonds that comprise each index. Composite Gaming Index represents the average market interest rate of over 80 corporate and Tribal high yield gaming issues

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borrow to fund the project. However, once the building opens – it follows that you use the cash flow generated to repay the debt. What is tougher is when there is an up-and-running business with a debt balance – and there is just interest due. In this case, the debt balance doesn't reduce. We think that in this economic environment, where there is more uncertainty, it makes sense to reduce debt whenever possible.

Many Tribes are looking to diversify away from their reliance on gaming, particularly considering the threat of competition seemingly always around the corner. It usually takes capital to enter into other lines of business. Reserves built up from casino cash flow are usually the best option for investment capital.

This tug of war is difficult to manage. The constant pull is from both sides – distribution vs debt reduction or reinvestment. What do we recommend tribes do when in this situation?

1. Develop a long-term plan. A 10 year plan will help identify risks in the cash flow generation and organize the tribe's priorities over time. This should include a strategy for debt repayment.

2. Work with your bankers, lawyers and advisors to construct refinancing alternatives in the case where debt loads and required service seems too onerous. Often, solutions to manage the situation to a more comfortable level of debt service are attainable if you approach the lenders in the right way.

3. Do a critical assessment of your operation – engage a "mystery shopper" or do a customer survey. Is a lack of maintenance a problem already, and, do customers notice?

4. Assess Tribal revenues and expenses as well to identify opportunities for growth and areas to reduce. It's best if reductions can occur over a longer period of time to allow for adjustments versus a knee-jerk reaction.

This is a tough topic. The answers may be right there in front of you, but difficult to act on. Make sure you address them though, before they start to affect the business or more importantly, the long term financial health of the tribe.

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