



*Margaritaville Biloxi – Why it
Failed...A Case Study*

Margaritaville Biloxi – Why it failed...A Case Study

Casual observation of the quick and complete failure of the *Margaritaville* project might lead observers to conclude that in large part the failure of that property was attributed to alleged Biloxi gaming market saturation. That is, the Biloxi market was at full capacity and the addition of *Margaritaville* in May 2012 was a matter of adding capacity to a market that was already at its tipping point. Closer inspection of the facts, however, will tell an entirely different story as is outlined below. In truth, the demise of *Margaritaville* was a business –not a market—failure.

Margaritaville Biloxi Profile

• Date opened:	May 22, 2012
• Date closed:	September 14, 2014
• Estimated budget:	\$62-65MM
• Casino square footage:	25,300
• Other square footage:	40,000
• Slots:	769
• Tables:	19
• Poker:	0
• Restaurants:	Two (<i>Margaritaville</i> and a buffet)
• Hotel rooms:	0
• Parking:	surface only
• Marina:	18 boat slips
• FY 2013 Gaming Revenues/Stats*:	\$21,100M
• Market share:	2.6%
• % of market positions:	5.2%
• Fair share:	39%

*estimates from MS Gaming data and other sources. 2013 was *Margaritaville's* only full year of operation

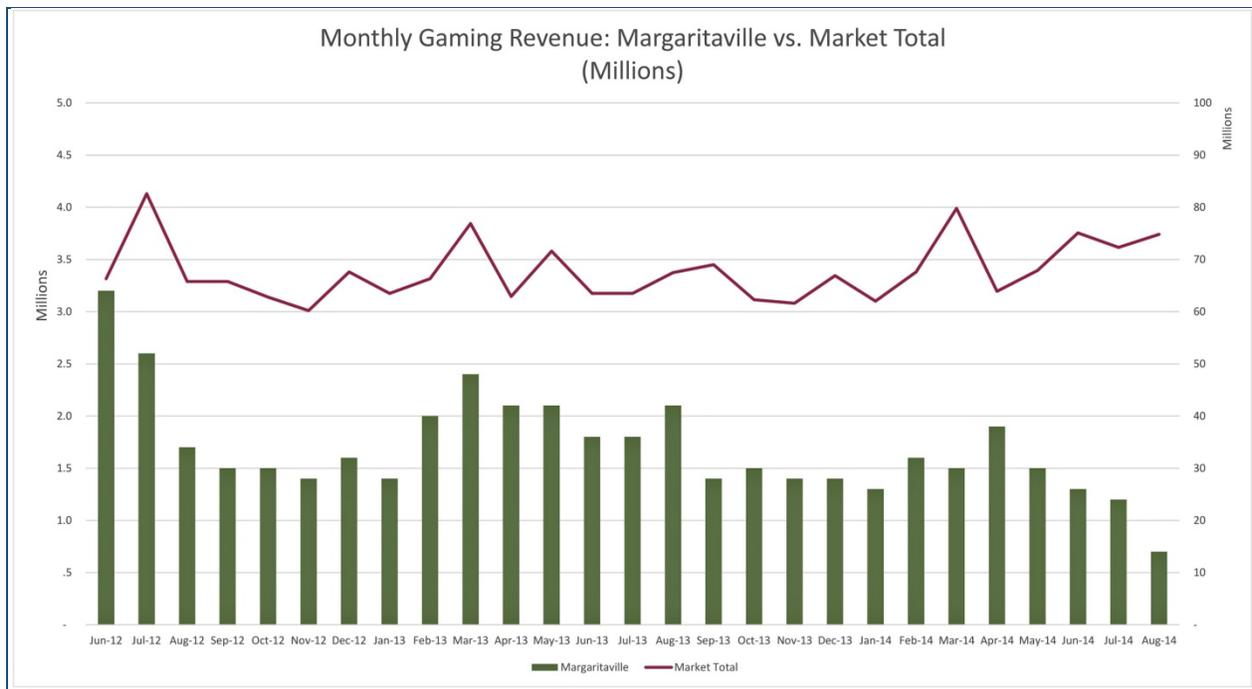
Margaritaville vs. the Market:

Margaritaville opened in May of 2012. For the Gulf properties gaming revenues for the full year 2012 were about even with 2011 (\$1.094MM vs \$1.096MM). Biloxi-only numbers were approximately \$828.2MM vs. \$824.9MM the prior year (Source: MS Gaming Commission and estimates)—modestly higher but not materially so.

In that context, *Margaritaville's* first month's revenues, at around \$3.2MM, were relatively good for a property with the second smallest (square footage) casino on the Gulf.

However almost immediately thereafter gaming revenues tumbled and never recovered. Beginning in 2014, as the graph shows, the overall Biloxi-area market begin to rebound with several factors driving that improvement including, most importantly, new investment in the Isle (metamorphosing into the *Golden Nugget* in three phases) and the expansion of the *Hard Rock*. Beginning in the Spring of 2014, the overall Biloxi market begin to strongly rebound however, *Margaritaville* didn't benefit from the general market improvement and in context its deterioration accelerated measurably to the point in September 2014 when it finally closed.

The key takeaway from a comparison of *Margaritaville's* performance vs. the market is that *Margaritaville's* performance—with fair share consistently at the bottom of the group—quickly dropped off following its opening and could never recover even when the rest of the market did. Moreover, the market's recovery in 2014 was in no way stimulated by *Margaritaville's* closing. Unlike Atlantic City where the reduction in the number of casinos has begat a cautious optimism that there is hope for that market's eventual recovery, *Margaritaville's* closing had no impact on the reality of the gaming business in Biloxi. That *Margaritaville* ever opened in the first place—let alone closed—simply didn't matter. The catalyst for Biloxi/Gulf improvement has been new investment in the market, strengthening national and regional economies, falling gas prices and the like. *Margaritaville*, with inferior product and customer experience all around, could not and did not benefit from the rebound when it began.



Margaritaville: Flawed Concept from the Outset

From almost the outset when the project was announced a number of analysts and observers expressed surprise that the project was seriously under consideration.

These individuals generally came to the same conclusion: over reliance on a very regional brand to carry the property, lack of logistical (road) infrastructure supporting the location of the property, a very constrained budget, the program parameters and the likely financing available would all contribute to the project’s ultimate failure. The project was financed on a budget and the final product showed it—and customers noticed immediately.

Moreover, the *Margaritaville* team ignored the very experts— **a nationally recognized gaming consulting firm** --they hired to model and assess the project and its ultimate viability. The firm’s projections, which supported the investment thesis in the first place, were predicated on a set of assumptions that, if followed or occurred (several assumptions were global in nature) could be reasonably expected to yield a successful outcome.

The major assumptions of the firm’s study dated August 2010 are outlined below along with an assessment of whether or not those assumptions were realized.

Nationally Recognized Firm’s Gaming Market Study key assumptions

<i>1. The Margaritaville Casino will be a high quality facility offering first rate amenities and services with FF&E similar to other developments in the comparable Biloxi markets</i>
RESULT: No, the property lacked many if not most of the amenities noted in the report assumptions; quality of the finishes were poor, gaming equipment was used (not new) and most amenities, for example the buffet which was added last minute to an unused, windowless space, sub par
<i>2. A professional and aggressive marketing program, including advertising and promotion, will be instituted prior to opening and maintained throughout the period of analysis</i>
RESULT: No, the property’s management was woeful and the marketing of the property weak to non-existent. Relied heavily on the Margaritaville name with little or no premarketing. No attempt was made to initially establish, for example, a data base or players club
<i>3. The property will have a highly competent and reactive management team to control costs and drive business</i>
RESULT: No, management was weak and lacked depth; they clearly failed to grasp the challenges extant in a new property. The COO, Karen Sock, departed after only three months following...never a good sign
<i>4. The future supply of competitive lodging facilities materially conforms to the estimates outlined in this report</i>
RESULT: Yes, the assumed supply was the same if not actually slightly less (<i>CanCan</i> was assumed to open in 2014—it didn’t) than assumed. Moreover, the quality of the project in the market improved with virtual same store improvements to the <i>Palace</i> and the <i>Isle (Golden Nugget)</i>
<i>5. Economic fluctuations will occur in line with assumptions herein</i>
RESULT: Yes, if anything, the national and regional economic circumstances relevant to the project were marginally better than assumed by Innovation—they was certainly no worse than assumed

The key factors which contributed to the collapse of Margaritaville are generally:

1. **Overly Strong Reliance On the Margaritaville brand** to carry the project. Management lacked vision of what the property needed to be in order to be competitive—they relied on a brand rather than the fundamentals of smart casino design and positioning
2. The **Scope of the Project** was very limited in size and awkward in configuration with a small, boxy casino serviced by only two restaurants and no hotel rooms; Gaming equipment was used (no new equipment)
3. **Operational/Marketing Issues** plagued the property from literally the outset. Management simply failed to appreciate the quality of product that needed to be built and how it should be managed. Strangely, no attempt was made to set up a player’s club or other means of tracking visitors and play.
4. **The Property site and related Infrastructural issues** made getting to the property a challenge and once there, somewhat difficult to enjoy. These issues, combined with an underwhelming visitor experience, meant that whereas initial trial was ok, repeat visitation was substantially lower
5. **The Project’s Capital Structure** extremely debt heavy and expensive. Moreover, land leases, equipment leases and high license fees (to Margaritaville Holding LLC) drained cash and flexibility. Lease and royalty payments alone were 12% of net revenues annually.



Source: Google Maps

Reliance on the Margaritaville Brand:

- The project’s developers, lead by CEO and ex-Grand Casino’s gaming vet Tom Brosig, believed that the strength of the Margaritaville brand would carry the project. Citing statistics which claimed that “55 million Americans bought the brand. That's 17 percent of the population”.

Brosig and his team believed that having a Jimmy Buffet “anchor” in his (Buffet’s) hometown region was apparently all it took to succeed.

- Observers noted that although the *Margaritaville* restaurant inside the casino held true to the brand, there was a marked lack of follow through with the rest of the property
- In addition, the royalty fee for the brand was a whopping 6% of net revenues
- Despite the licensing agreement, sources suggest that unlike *Hard Rock Biloxi*, *Margaritaville* gained little from the arrangement in terms of data base instead relying on word of mouth and more casual references to the property on the Margaritaville website

Scope of the Project:

- At around \$65MM the budget for the project was believed to be too low to build a competitive property
- At 65,300 combined square feet, the property would be the smallest on the Gulf by a wide measure (*Treasure Bay* at 83,813 square feet is #2)*
- At 769 slots it had the second fewest slots in the market (*Grand*, at 754, had the fewest)*
- Moreover, the casino at 25,300 would be the second smallest. Only *Golden Nugget*, at 23,787 is smaller however, GN has more gaming positions, a far larger overall footprint and 550 hotel rooms*
- There are no hotel rooms—those would come in a subsequent phase
- Initially the project was to include only one restaurant, a *Margaritaville* concept. Only toward the end of construction was a buffet added in what was to be an employee space. Hence the buffet area included no windows to the outside
- The building sits on stilts in order to comply with FEMA requirements post Katrina. Primary access to the casino from the parking lot is via (covered) escalator or stairs
- Parking is entirely surface and in an elongated parking area in front of the property (see photo)
- A tiny 18 slip marina was too small and according to boaters, lacked sufficient baffling to adequately protect boats from strong currents unique to that location

*Source: Mississippi Gaming Commission 12/31/13



The Site (Oak Street on the far left, 5th Street at the bottom)



Source: Google Maps

The Marina and beach areas



Source: file and Google Maps

Operational/Marketing Issues:

- The property opened with no data base and no direct mail program.
- No player club existed and initially no attempt was made to establish one. Local players therefore had little incentive to return—and didn't.
- Signage (inside and out) was described as “weak”.
- Virtually no material signage on the key approaches (Bayview Ave/Back Bay Blvd and Hwy 90) to the property.
- Physical finishes were subpar with observers noticing problems with drywall and other details.
- Gaming equipment was leased and was second hand equipment. Presumably this was done to save costs but given the cost of the leases themselves clearly hurt not only player reception but the bottom line directly as the leases were rumored to be in the range of 15%

Casino detail (left); Casino floor

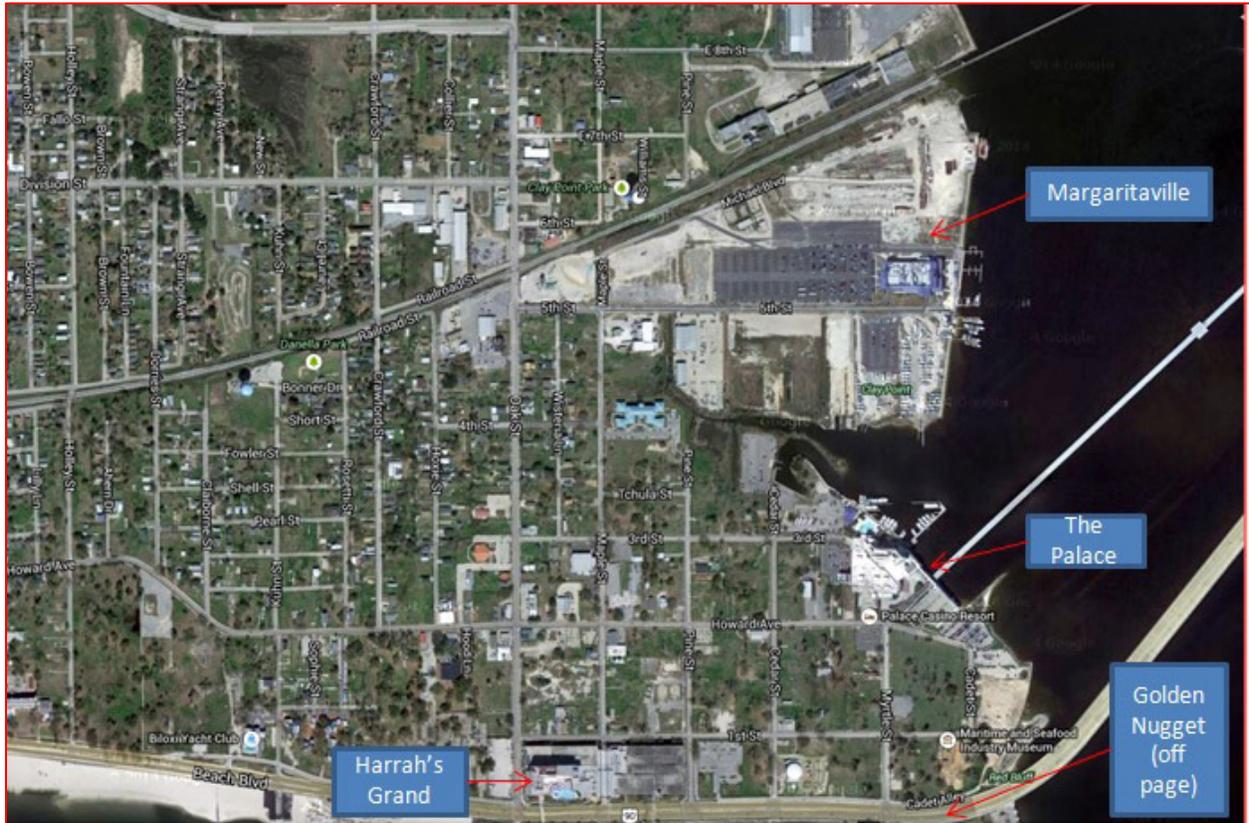


Source: TripAdvisor

Project Site/Infrastructure Issues:

- The property sits by itself on the eastern edge of Biloxi peninsula facing Biloxi Bay
- The property's relative isolation is not dissimilar to most of the Biloxi casinos in so far that few properties other than the *Beau Rivage* and *Hard Rock* are truly contiguous; *Margaritaville's* location is uniquely problematic however because of the lack of logistical infrastructure to the site. The main access road from the north side of the peninsula, Back Bay Blvd., ends almost a half a mile from the property with access limited to poor two lane surface streets. Access from the south (Highway 90) is also on a (better) two lane surface street and extends for over a mile
- The last quarter of a mile to the location runs by a rock quarry, a light industrial area, vacant land and a boat storage yard—hardly creating a unique “sense of arrival”
- The property's logistical complexities were made more difficult by a singular lack of signage marking the location of the property including clear directions as to how to get there.
- The lack of a high-rise hotel structure also limited the property's line of sight from almost anywhere on the peninsula or Interstate 110 (a key arterial connecting Interstate 10 to Biloxi). Important “free” advertising was therefore unavailable to the property
- The property was constructed on leased land. Not only were the leases expensive but also by extension meant that the owners didn't control a key asset. In fact, when the property closed in September 2014, ownership cited failure to negotiate an “agreement” with the landlords, likely for lease relief but ostensibly for permission to build a hotel on site, as a major contributing factor precipitating closure (<http://www.wlox.com/story/26539317/margaritaville-casino-closes-in-biloxi-350-out-of-work>)

Eastern Biloxi Peninsula showing landlocked location of *Margaritaville* site



Source: Google Maps

The *Margaritaville* restaurant and buffet



Source: TripAdvisor

Capital Structure/Financial Issues:

- The project was largely funded via very expensive debt and operating leases. Very little equity was utilized—an estimated \$15MM out of a project budget of around \$65MM (around 23%).
- Moreover, almost all of the FFE including gaming equipment was leased. Estimates on the cost of the leases were 15% or so
- The lease package was believed to be \$23MM of the capital structure with another \$18MM in senior debt included in addition
- Apparently no liquidity cushion was provided for and sources suggest that the project commenced construction without all of the sources of capital being identified. By the later stages of the project funding shortfalls were apparent. PDS Financial, provider of the gaming equipment and other FFE, is rumored to have provided an incremental \$5MM of capital as a stop gap
- In addition, sources also indicate that somewhere between \$3-6MM was “provided” by the contractor and others involved with the project in an effort to close the funding gap. This unexpected contribution to the project was likely made via deferred fees and recorded as equity
- The land itself was also leased from a consortium of land owners with a 100 year lease signed paying 6% annually to the lessors
- The Margaritaville brand license fee was 6% of net revenues
- Revenue assumptions and margins were very aggressive. 2013 gaming revenues, for example, were forecast to be just under \$70MM. The actual revenue total for 2013 was only \$21MM. Achieving these numbers, as pointed out, were predicated on a number of assumptions made by the consulting firm; however, those assumptions which were under the control of management were largely ignored de facto



The “Fin” came quickly for Margaritaville

Conclusion:

Margaritaville Biloxi was a project that should never have been built as it was flawed from the inception by its faulty design, capital structure and poorly conceived business plan. That it was is as much a reflection of the times with money available at some price for any concept that only had to *seem* reasonable. The development/management team's naïve reliance on a particular brand to carry the project to what they anticipated to be superior returns while ignoring the fundamentals of casino marketing, casino design and logistics proved nearly fatal. The project's capital structure with high interest on debt and chunky lease payments (for nearly everything in the casino was leased), a low equity base, little contingent liquidity and crushing land lease and royalty payments assured failure.

The project's failure was so embarrassing to the State of Mississippi that it was a contributing factor to a wholesale revisal of the State's requirements for new property investments. Beginning January 1, 2014 the State would require new casino projects to meet investment minimums in terms of hotel rooms (300 minimum), casino square footage (40,000), car garage (500 stalls), fine dining restaurant (75 seats)—these and more to also include a “unique” amenity of undetermined scope and content.

Margaritaville's failure is a commentary on misguided intentions and woefully poor execution. What it isn't is a reflection on Biloxi market gaming saturation. The addition of *Margaritaville* had little impact on the competition's performance one way or the other and the market revenue numbers support this view. The Biloxi market began a strong recovery in 2014, however for *Margaritaville* it would come too late to stave off the inevitable consequences of a number of bad—and ultimately—fatal flaws in design and execution.

***“Wasting away again in Margaritaville,
Searching for my lost shaker of salt,
Some people claim that there's a woman to blame,
But I know, it's my own damn fault.”***

--Jimmy Buffet

