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A Perspective on Racing — As I See It

Moderator/Speaker:
Ron Geary, President and Owner Ellis Park Race Course

MS. WENDY DAVIS: Good morning. Welcome to the second morning of the Symposium on Racing for 2007, thanks so much for being here. Just a few housekeeping announcements before we start, we'd certainly like to thank AmWest Entertainment for breakfast this morning. Also, we'd like to remind you that this afternoon from four to six is the showing of the movie, The First Saturday in May. I understand that it's wonderful; it's one of those things that I don't think you're going to want to miss.

And also, tomorrow, don't forget to put on your calendar the Race Track Industry Program students will be presenting their projects, these are the projects that were done in the capstone course, and they will be right outside here in the foyer and that will be tomorrow morning.

This year we started a new theme and that's "A Perspective on Racing, As I See It," or as we see it. It was an idea that started to get kicked around at the Race Track Program, and we said it would be really interesting to bring a number of different people in and different perspectives and just see how someone looks at our business. This morning we have Ron Geary, president and owner of Ellis Park Racetrack as our guest to give you his perspective on racing. Mr. Geary has served as president and CEO of ResCare as well as president and consultant to the Cincinnati Bible College and Seminary. Prior to that he served in government as Kentucky's assistant secretary of state from 1989 to 1990 as well as secretary of the cabinet of Jefferson County from 1984 to 1985. But what's really important here is that he is an owner of a racetrack who is also the owner of thoroughbred horses, I know I certainly appreciate that as an owner of thoroughbred horses. Without any further ado, please welcome Mr. Geary up as our first speaker of the day. Thank you very much.

(Applause)

MR. RON GEARY: Thank you Wendy, I do appreciate the opportunity to be here this morning to talk about an industry of which we all have a passion for and love. As Wendy mentioned, I'm here as a small racetrack owner as well as the owner of four thoroughbreds; one of them is retired, I might add. Also I think that I'm representing, in some way, the handicappers throughout the country, as that has been a hobby of mine for a few years and one that I enjoy, some of the handicapping contests. And I also got to know and appreciate a lot of the perspectives of the horseplayers. As you know, one of the emphases of Ellis Park this last year was to focus and to be considered the horseplayer-focused track and I think that we've done a pretty good job of doing that.

So I've got a lot to cover as I kind of review my perspective of racing, as I see it from all my different hats that I wear. Before we do this, I'm going to run a little clip here that I think we can learn some things from.

(A videotape was played)

I wanted to show you that because, number one, I think that as we, as an industry, as we look around, we're looking and fighting in a lot of different areas, but as an industry, we've got to stay focused with our head looking ahead. I actually saw that in another place and it was just so funny, I had to work it in somehow.

The truth of the matter is, though, I think we do need to focus as an industry and hopefully that will show you if you're not staying with your eye on the ball, bad things can happen to you.

What I thought that I would do is kind of give you my perspective, I'm kind of data-oriented and I'm focused a lot on financials and information like that. What I wanted to try to do is try to give you a little bit of a micro view of how I see the industry, let the figures speak for themselves and then kind of focus a little bit lower and then finally focus in a little bit on the Ellis Park experience. And then kind of come up with an idea that has kind of evolved as I've worked through getting some of the research done.

First of all, I think that everybody's aware from the chart here that as an industry we've really been looking at -- wagering has kind of been stagnant, that's maybe the nice way to say it, it's kind of been flat. Hovering right at $14.5 million to $15.1 billion in handle. I think that you can see that that goes from 2001 and I've estimated 2007, I've used the Equibase figures that I have a lot of confidence in. Actually I've issued my first official estimate of revenue; I've looked at the first three quarters in 2007 and estimated that 2007 is going to probably be flat for the whole year, as far as handle.

So I think, from my perspective and the company that I grew for 16 years, you might of heard of it, it was a NASDAQ company called ResCare, we provide services for people with developmental disabilities, we're the largest in the country and I was involved in growing that company from $60 million a year that we now do $1.5 billion a year; I'm still chairman of the board of that company, having retired last year as president and CEO. And one of the things that we've done as a company every year in our strategic planning sessions, one of our major principles is a book called Double-Digit Growth. And if you're going to survive, if you're going to grow, if you're going to prosper, you need to try to focus and find away to get double-digit growth. Obviously, as an industry we're not doing that, and obviously the individual components that make this up, many of us are not doing that either.

So from my perspective, as a lesson learned looking at the strength of ResCare, where we say, we grew from $60 million a year to $1.5 billion a year, is now our annual revenue, that results in a lot of spin-offs for other opportunities, because when I got involved with ResCare we had 1,500 employees in five states, today we have 42,000 employees in 34 states by trying to follow the principles that are in this book, pretty basic stuff. But I think we as an industry need to give some real consideration as to how we can try to move into double digit growth, it's not going to be easy, but I can tell you right now, there's a lot of potential handle out there in the gaming industry that we're missing out on.

So that is my first observation, that we need to do a better job of trying to get some growth into our industry, the figures are there, we're flat as far as an industry, I think everybody knew that, this kind of documents it officially.

What about our purses that we offer? The next chart, you can see, it's been substantially flat. However, there is some movement in this, 2006 was up about three percent over 2005. What it looks like, again, projecting 2007 out after the first three quarters, recapped by Equibase, it's looking like it could have a six or seven percent increase, and a lot of that is attributable to the Presque Isle, the new operations and purses are pretty substantial. But also the footnote on the bottom shows that Louisiana, Pennsylvania as a whole, not just Presque Isle, West Virginia, New Mexico, Florida and Delaware have started the momentum that is helping finally to start picking up the growth in purses. Certainly this is a movement in the right direction and one that we should be proud of, but also learn that the bulk of that is attributable to alternative gaming, as these states have brought about the racino's and casinos in their states to assist the thoroughbred horse industry.

The next thing I did, I wanted to focus in a little bit more, I looked at the micro, so this is kind of a reduced micro approach. I wanted to look at the top four publicly held companies that are in our industry and what are their comparisons, how do they compare with each other? If you can look, I went with Magna, Churchill Downs, Penn National, Youbet, and I tried to get TVG figures, as you know, they are kind of a subsidiary of a large publicly held company called Gemstar International. The figures are just not available broken out in any significant, meaningful way, at least for the two years that I looked at. Having run a publicly held company for 16 years, I appreciate the pain and suffering it takes to work through all of the preparations of 10Qa and 10Ks and therefore shockingly and surprisingly and sadly I enjoy reading those. Of course, it is kind of like handicapping horses sometimes, you handicap companies the same way. But to show you some of the comparison and to give you a snapshot, we have flat sales as an industry, how are some of our bigger players doing? Well, you can see revenue, the top line, the trailing 12 months, Magna has $735 million in revenue, Churchill is $402 million, they used to be more than that but with selling off three of their operations in the last several years, their actual run rate has declined somewhat. Penn National, I've always known of Penn National but once I did this comparison I was pretty surprised as to how strong they are in terms of revenue and balance sheet, but you can see they do $2.4 billion a year in revenue. Youbet is $142 million run rate and TVG is really not available although the revenue figures are, and it appears that the revenue figures for TVG would be between $55 and $60 million a year in revenue.

Now, the market cap is another major -- the second set of figures there. This is what number of shares outstanding by the current price and so you can see the market cap, market value of Magna is $170 million, based upon a price down there, fifth set of figures, $1.46 a share; this is as of last Friday. Churchill has a $718 million market cap, very strong, a good price of $52.48. Penn National is at $5.2 billion as far as market cap and they are in the process, they are trying to go private, they have a contract with some private equity folks, I think the purchase price is about $6.1 billion, something like that, and there are a lot of regulatory approvals that have to be made, but you can see their current price is $59.55. Market cap for Youbet is $47 million. The stock price currently, or at least on Friday, was $1.12.

Now, the next figure is EBITDA, and as I would do road shows for ResCare on Wall Street, I often wondered what EBITDA was and at one point I kind of came up with a simple approach as Arabic for cash flow. What it really stands for is earnings before interest, taxes, depreciation and amortization expenses and really it's kind of cash flow from operations before you're debt service and taxes is what it looks like. So you can see that Magna has a negative EBITDA of $21 million, that doesn't bode well with the next line that shows that their total debts is $586 million, because you're supposed to be paying the debt service or your debt back out of your EBITDA, so that causes a lot of concern as I know everybody knows that already.

Churchill Downs, on the other hand, has a very strong $56 million annual EBITDA and only a total debt of about $69 million and a lot of that was just incurred when they bought Brisbet, some of the other AmericaTab companies for about $80 million, I believe, they incurred some debt there. Of course, they used to have more debt than that but when they sold Hollywood back a few years ago, for I think $250 million that allowed them to reduce their debts substantially.

Penn National, on the other hand, has $2.9 billion in debt, and you say, well, that's a lot of debt, but when you have the EBITDA of $638 million a year, that means that your EBITDA in comparison to your total debts is a little bit, 4.1 or 4.2 multiples is not a dangerous or high level, it's satisfactory, if you've got cash flow, you can kind of stretch yourself a little bit more in debt. But obviously the growth and the revenue of Penn National comes greatly from their successful movement into the casino and racino business, it's obviously served them quite well.

And then you can see Youbet has $20 million in debt and a $6 million EBITDA, which covers about 3.2 multiple of debt to EBITDA.

Finally, the total stockholders' equity for each of the companies is $401 million for Magna, which, with them having lost about $400 million in the last several years, that reduced it, so their original capital was, I think, satisfactory, it was moving and assuming a very strong base. But obviously they did not anticipate the substantial losses that they've incurred. Churchill has a very strong balance sheet, again, with strong stockholders' equity of about $350 million. Penn National, $921 million stockholders' equity. And Youbet has $53 million.

So I thought, again, as I wanted to give you my perspective as a businessman, I always kind of look, I go to the Internet, I go to 10Ks, 10Qs, and I've given you the macro approach, it's not a really strong picture. You look at two of our four publicly held companies have some serious concerns about their financial performance.

The next thing that I wanted to look at was to kind of focus in, a micro look at Ellis Park. Now, when I bought Ellis Park, I just retired from ResCare, I had been blessed with the financial performance there, and even though I always want to try to strive to make it a successful investment, it had seven years or so of continuing accelerating losses. So I didn't have a lot of high expectations, but my goal was to try to get it to breakeven in three years. But most importantly, I wanted to kind of use it as a laboratory for the Kentucky thoroughbred industry as well as for the national industry to see if we could come up with some ideas that might be of help somewhere, somehow along the way. I will say that the hope of getting to a three-year breakeven, I think, is still there, I think it's going to be more difficult as Indiana has gotten slots in their two racetracks, Pennsylvania has opened up Presque Isle as well as the continuing strong states of West Virginia, Illinois also has some forms of gaming, that's making it more and more difficult for Kentucky to maintain their strong role in the thoroughbred horse industry. …….**Other terms, concepts and keywords contained in the balance of this transcript are:** TVG, TrackNet, Magna, Churchill, CDSN, distribution, Youbet, Claiming Crown, glow effect, partnership between horsemen and track, horseplayer, four percent takeout Pick-4, gaming, legislature, free market, maximum content availability, maximum signal distribution, centralized betting exchange, Equibase, nonprofit charter, cap return……..If you desire a full transcript contact bprewitt@ag.arizona.edu