

Trump Entertainment Resorts, Inc¹

Assignment for First Class

It was Thursday afternoon May 25, 2006. Jennifer Chang was sipping her tea and reflecting on the Deutsche Bank's buy recommendation for Trump Entertainment Resorts (TER, NASDAQ ticker: TRMP) that came out on May 24th. TRMP closed at \$20.24 (closer to the 52 week high of \$21.72 than the low of 15.88) on Wednesday May 24th whereas Deutsche Bank's price target was \$25. Jennifer joined Disciplined Asset Managers as a junior analyst in July 2002 soon after graduating from one of the Ivey League universities with a triple major in English, Mathematics and History. She rose rapidly to become a portfolio manager with \$500 million of assets under her management, and is viewed as a rising star among fund managers who use the Value approach to investing.

TER owns and operates three casino hotel properties in Atlantic City, New Jersey: Trump Taj Mahal Casino Resort (Trump Taj Mahal), Trump Plaza Hotel and Casino (Trump Plaza), and Trump Marina Hotel Casino (Trump Marina). TER conducts gaming activities and provides customers with casino resort and entertainment experiences. The company's net revenue in 2005 was \$992 million.

Recently, the real estate prices in Atlantic City have been on a rise:



Figure 1: Average sales price for homes in Atlantic City. Source: trulia.com

http://www.trulia.com/real_estate/Atlantic_City-New_Jersey/

and hotel companies have become very attractive to investors, selling at multiples as high as 18 times cash flow²

¹ Prepared by Andrei Jirnyi and Soohun Kim under the guidance of Ravi Jagannathan. ©2010 Ravi Jagannathan

² "Casinos: Divide go Conquer", Peter Sanders, WSJ, January 23, 2007

Comparable properties have been sold at prices between \$3.2 million/acre in downtown locations (such as Trump Marina), and \$3.5 million/acre on Boardwalk (where Taj Mahal and Plaza are located). The hotel properties, if valued at \$300,000 per room, would come up to \$853 million – excluding any value that one could derive from the main casino operation itself.

Based on a cursory review, Jennifer decided that TER deserves a closer look.

Come prepared to discuss the following questions. However, do not spend too much time on any one question, just think about the issues involved and come prepared.

1. Open [facility_stats_2005_2007.pdf](#). Based on the information in the file, compare Trump Marina, Trump Plaza, and Trump Taj Mahal with Caesars AC, Bally's AC and Borgota in terms of number of rooms, and casino area in 2005. How large are the Trump facilities relative to others?
2. Based on the Trump Annual Report for 2005: What percentage of the total revenue came from Gaming?
3. What are the components of Trump's intangible assets(Read the Annual Report of Trump for 2005)?
4. Read Hurrah's Entertainment Inc AR 2005, Form 10-K, page 32. How much did Hurrah's pay for Caesars Entertainment in 2005? How much of it was for goodwill?
5. Read Hurrah's Entertainment Inc AR 2005, Form 10-K, page 2. Compare the size of Ceasars to that of Trumps in terms of number of casinos, rooms and gaming space. What would be a reasonable range of values for intangibles of Trump?
6. Make suitable assumptions and compute the Adjusted Asset values for Trump. Group your adjusted asset values separately for Current Assets, PP&E, and Intangibles. Based on your computations, do you think Trump is a Net-Net stock?
7. Suppose your estimates for adjusted asset values are off by 3%. How would your conclusions change?
8. What is the value of leveraged firm according to Miller-Modigliani?
9. What is the WACC of TRMP under the current capital structure?
10. What would be TRMP's WACC if it had the capital structure of the industry as a group?
11. Do you think the operating income of 2005 is representative? Why or why not?

12. What adjustments to the operating income of 2005 would make it more representative?

13. Compare the historical trend in gross operating profits (GOP) of TRMP with that for other casinos in Atlantic City.

14. Consider the following equation for GOP:

$$\text{GOP} = b_0 + b_1 \cdot \text{Number of Rooms} + b_2 \cdot \text{Number of Tables} + b_3 \cdot \text{Number of Slots} + \text{Error}$$

Estimate the coefficients, using data for all the casinos and based on your estimated values for the coefficients, compute the predicted value for GOP of TRMP. You need to use the data in Annual Stats 2000-2008websitepost.XLS, facility_stats_2005_2007.pdf, and casino_facility_stats_1981_to_2004_years.pdf. You can download facility_stats_2000_2005.xlsx from course website which summarizes the two pdf files. Use 2000~2005 data to fit the suggested equations. Also, note that Claridge merged with Bally's AC effective January 1, 2003. Hence, you should consider those two companies as one.

17. Which of the Trump casinos are better/worse based on your predicted value for GOP?

Data sources

You main source of information will be the 2005 Trump Entertainment annual report, available from the company's website. More company statements can be found at EDGAR website – in particular, Edgar/PriceWaterhouse EDGARScan provides a nice interface to this database. Online services (free or low membership fee) often provide easy access to current financial information (Yahoo Finance, Google Finance, and Reuters.)

The website <http://www.state.nj.us/casinos/financia/histori> gives statistical information on Atlantic City casino industry. Click 2000-2008 and download Annual Stats 2000-2008websitepost.XLS; click 2005-2007 and 1978-2004 and download facility_stats_2005_2007.pdf and casino_facility_stats_1981_to_2004_years.pdf in Facility Statistics.

These and other relevant files -- Trump_2005_AR.pdf; Annual Stats 2000-2008websitepost.xlsx; facility_stats_2005_2007.pdf; facility_stats_2005_2007.xlsx; casino_facility_stats_1981_to_2004_years.pdf; Hurrahs_2005_AR.pdf; as well as the Deutsche Bank's initiating coverage report on TER, deutsche_060525.pdf, S&P_Industry Surveys_Lodging&Gaming_060202.pdf -- are also available on Blackboard.

Table 1 below gives the debt/equity mix for a few firms in the gaming industry. Table 2 gives the stock and asset betas of those firms.

Table 1:
Capital Structure of Companies in the gaming industry

Company	Debt[1]		Equity[2]	
	\$M	D/(D+E) %	\$M	E/(D+E) %
Harrah's Entertainment, Inc.	11,039	46%	13,105	54%
Trump Entertainment Resorts, Inc.	1,408	72%	547	28%
Boyd Gaming Corporation	2,559	38%	4,256	62%
MGM MIRAGE	12,355	54%	10,454	46%
Average	6,840	52%	7,090	48%
Weighted average		49%		51%

Source: Annual Report of Each company, Yahoo finance

[1] Long Term Debt, less current maturities

[2] Common stock price × The number of outstanding shares at 12/31/05

Table 2 :
Beta and Debt yields for firms in the gaming industry

Company	Beta, 03/31/06		Debt yield
	Stock	Assets	
Harrah's Entertainment, Inc.	0.81	0.44	5.87%
Trump Entertainment Resorts, Inc.	0.31	0.09	8.98%
Boyd Gaming Corporation	0.92	0.57	7.37%
MGM MIRAGE	0.87	0.40	6.89%
Average	0.73	0.37	7.28%
Weighted average	0.83	0.43	6.58%

Source

Bloomberg LLP