

# *Managing Revenues in Macau's Casino Resorts through Turbulent Times: A Case of the "New Normal"?*

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## **Introduction**

Since it was introduced in the hospitality field, the revenue management (RM) function has played the lead role in maximizing room revenues for many industry operators. Following Macau's return to China from the Portuguese colonial authorities in 1999, the hospitality sector has developed rapidly, with the casino segment being the major contributor to hotel revenues. In this context Revenue Management has become a more strategically oriented means of optimizing total revenues, particularly in the context of integrated resorts which encompass wide-ranging hospitality functions. As well as involving the management of rates, this approach extends to resort branding, positioning, and understanding the impact of generating room nights for other revenue centers. This case study presents the prevailing circumstances in Macau – a "special administrative region" (SAR) within greater China - where casino resorts are confronting an economic slowdown and intensified competition. The following key question is posed – how can a new casino resort identify and establish a strategic positioning in the face of such challenging market conditions?

The following section provides some detailed background about market conditions in Macau. This will assist students to appreciate the types of decisions about pricing and revenues that are needed in a city tourism economy where gaming is prominent. There is growing competition for all cities that feature tourism and gaming. If they are to attract more high yielding visitors, they must find a balance between the gaming and non-gaming components. By explaining the conditions that prevail in the Macau market, this case study provides insights that can be applied in other parts of the world.

## ***The Growth of Tourism in Macau***

Macau is a 30m<sup>2</sup> city located in southern China, adjacent to Hong Kong (another SAR). In the 1990s and prior to the so-called handover in 1999 when Macau was still a Portuguese colony, the Chinese government started to relax the prevailing restrictions on foreign business operations. In the face of this major structural change, most Macau factory owners opted to relocate their production to China with of view to benefiting from the lower cost base. This business exodus prompted

tourism and gaming to become the main pillars of the Macau economy.

Following the globally significant Severe Acute Respiratory Syndrome (SARS) outbreak in 2003, tourism demand collapsed. To support the economies of Macau (and of Hong Kong), the Chinese government implemented the Individual Visit Scheme (IVS), hoping that tourism growth would stimulate other industries and avert the downturn. However, the tremendous growth of tourist arrivals which followed was unanticipated. Tourism arrivals grew by almost three-fold over the following decade. Driven primarily by policies that were formulated in China, the bulk of the growth of arrivals has emanated from Mainland China, followed by visitation from Hong Kong and Taiwan. These three sources collectively account for over 90% of visitor arrivals (DSEC, 2016a). This has resulted in a close relationship between the tourism sector and the political and economic environments prevailing in the three major source markets.

## ***Macau's Casino Market***

Casino operations were legalized in Macau in 1847 during the Portuguese colonial period (DICJ, 2016). Macau is small and lacks natural resources and it is the gaming and tourism sector that has emerged as the tiny city's main economic driver. There are currently six casino operations: SJM (which is locally based and a subsidiary of STDM), Sands (USA), MGM (USA), Wynn (USA), Melco Crown (Australia) and Galaxy Entertainment Group (Hong Kong).

The introduction of IVS boosted tourist arrivals to record breaking levels and attracted billions of dollars in gaming revenues from so-called "high rollers". It has been reported that the first casino hotel to be built by the new concessionaires, namely Sands Macao, a 5-star hotel with 289 suites, recouped its investment costs within 9 months of opening in 2004 (Cohen, 2014). Macau attracted international attention in 2006, when gaming revenues exceeded those of Las Vegas, the long established global casino leader, only 4 years after the liberalization of casino operations. Macau's total gaming revenues continued to break records for 11 consecutive years, rising from USD \$2.9 billion in 2002 to USD \$45.2 billion in 2013. The remarkable growth seemed unstoppable, until the successive formulation and implementation of China's Anti-Corruption campaign in 2014. As a consequence of the new policy, high rollers kept a low profile and reduced their visits to Macau. In 2014, Macau's total gaming revenues experienced their first ever year over year drop to USD \$44.1 billion. The uncertain conditions

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continued and in 2015 the numbers dropped further to USD \$29.0 billion. It remains uncertain how long the current trend will continue.

Each of the major casino operators has new properties under construction and these fledgling operations are confronted by a confluence of factors. These include delays to government approval processes, a tighter bank financing environment and operator hesitation about how to react. Meanwhile it has been reported that the opening dates for most of the new properties have been delayed. The respective operators are aware that the market may not recover in time to coincide with the property openings. Macau style gaming is currently characterized by high rollers and luxury surroundings, but reduced spending power amongst the newly arriving tourist groups has meant that it is critical to implement a revenue management plan which gives the newly opening properties the best prospect of attaining competitive advantage.

### ***Macau's Hospitality Market***

The growth of Macau's hospitality industry has been characterized by increasing visitor arrivals and by the development of casinos. While there were only 35 hotels offering 8,200 rooms in 2002, this had grown to 66 hotels offering 32,200 rooms in 2015. In light of the many properties currently under construction, it is anticipated that the number will rise progressively to 50,000. In the first years after the liberalization of gaming, the newer casino hotels were located in peninsular Macau, near the city center, heritage sites and existing hotels. However, the overall operating environment has been transformed by the progressive expansion into resort-style casinos. All casino concessionaires have committed to property developments on the Cotai Strip – a replica model of the Las Vegas Strip on a reclaimed section of land that combines the names of two previously separate islands – Coloane and Taipa. As the focus of the various integrated casino resorts, it may also be viewed as a competitive "battlefield" where long term success will be determined.

The hospitality sector has developed well beyond hotels and rooms. Recent additions have included world class entertainment, a diversity of food and beverage outlets including at the top end, a huge capacity of MICE facilities (Meetings, Incentives, Conferencing/Conventions, Exhibitions/Expositions and Events), family oriented facilities and retail experiences. These various elements have transformed hotels into integrated resorts, offering options to a range of market segments, and extending the duration of stay amongst guests. There are currently 16 hotels on the Cotai Strip that are operated by the casino concessionaires. Of these, 9 are rated as 5-star or above and account for some 80% of the room inventory. Of the seven additional hotels that are under construction, 4 are planned as 5-Star or above. The boom of hotels in the 5-star and 5-star luxury categories has been supported by the high average gaming expenditures by VIP players. These are retained with the support of offering complimentary rooms, depending on their gaming ratings. These 5-star hotels and casinos

have worked collectively to develop the so-called premium market. Appendix Table 1 presents the details of different Cotai Strip resort complexes with their star rating, room inventory, and Best Available Rate level and featured facilities.

The current market environment is very challenging for the various operators. The changing nature of tourist groups, has led to significant drops in average per player gaming expenditures when total gaming receipts and tourist arrivals are viewed collectively. It is worth considering whether to maintain the premium pricing strategy of high prices and commensurately high quality, or to shift to a penetration strategy of high quality but lower price. It is evident that casinos now need to capture more low rating players if they are to sustain their operations, and to improve the utilization of assets by filling the hotel rooms. In light of the continuous growth of hotel capacity, a more concerted effort is required to sell the rooms to the non-gaming market, even as the gaming market is slowing and experiencing a downturn. In Appendix, Figure 4 and 5 indicates the average length of stay for tourists to Macau; and, Tables from 2 to 6 demonstrate the buying behaviors of current visitors to Macau.

### ***Case study questions***

Students should group into teams and work on the questions that are noted below.

Please consider the opening of a new development project which is scheduled on Cotai Strip for two years from today's date. The complex will feature a 1,000 room 4-star hotel, food and beverage outlets, convention and exhibition facilities, and some retail. The new property will complete in the competitive market that is set out in Table 1.

1. Considering the proposed facilities within the complex that are suggested above, please describe your intended target market(s).
2. Which customer needs merit greatest attention, in light of changing tourist arrival patterns?
3. Please indicate which of the hotels that are listed in Table 1 potential competitors are. Using Best Available Rate for comparison purposes, what rate positioning would you suggest for your proposed hotel?
4. Given the likelihood that it will take several years for market conditions to recover fully to Macau's 2014 peak, how do you suggest that the new hotel should position itself to maximize its competitive advantage?

### ***Questions for further discussion***

- Beyond the casino operator developments outlined in Table 1, what support facilities may be required to support Macau's growth as a tourism destination?
- What initiatives could be implemented by the Macau government to support the recovery of the tourism sector?

- If a potential investor proposed to develop a non-casino hotel near the various complexes in Cotai, what are your suggestions for an appropriate room inventory, facilities, target market and rate positioning?

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## *About the Casino Concessionaires*

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- Galaxy Entertainment Group - [www.galaxyentertainment.com](http://www.galaxyentertainment.com)
- Melco Crown - [www.melco-crown.com](http://www.melco-crown.com)
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