

Eating and drinking enriches us

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Although dining has long been an unimaginative diversion from the gaming that was the central activity here, diners now have a wide array of options from fine dining to pub grub that was unimaginable a generation ago.

While the variety makes establishing a personal favorite a more exciting challenge for tourists and locals alike, everyone agrees that, on the whole, perhaps the best dining in the United States can now be found in Las Vegas.

The feeding frenzy easily translates into big business. According to the National Restaurant Association 2004 Industry Forecast, Nevada is projected to lead the country in restaurant sales growth, while the Nevada Restaurant Association expects the industry to gain more than 105 new restaurants, a rate of two every week, to the county's current inventory of about 1,300 full service eateries and 3,500 total eating establishments.

Although presenting consumers with more intriguing choices than ever before, the explosion in Las Vegas dining means large opportunities for entrepreneurs with the stamina and wherewithal to take the heat in the kitchen.

The pitfalls are, however, numerous in an industry that probably has the highest failure rate among new businesses in the first three years of operation than any in the country. Competition in the Las Vegas market is especially keen, as local independent restaurants face chain outlets arriving in droves with deep corporate pockets that can secure scarce prime locations and ride out any tough times.

"We really are a maturing market," says Van Heffner, president and CEO of the Nevada Restaurant Association, which has over 1,000 restaurant and supplier members representing over 60,000 employees. "Twenty years ago, we were the buffet capital. Now we have gourmet. The finest eateries around the world have a presence in Las Vegas. What is interesting is the new cuisines and fine dining restaurants. The level of sophistication, from presentation to fresh product to style [is superior]. The fine dining experience that some had in Paris, France, they can now have in the Picasso in the Bellagio."

As gauged from tax revenues, food and beverage sales in Clark County totaled \$501 million in January alone, a hearty 15.4 percent increase from the \$424 million spent in January, 2003. Between last July and January, food and beverage revenues totaled \$3.2 billion, a zesty 11.5 percent hike from the \$2.9 billion expended over the same period last year.

The phenomenal growth experienced in the restaurant business here probably matches any other place that generates such a high volume of foot traffic over a concentrated area. According to the Las Vegas Convention and Visitors Authority, the average tourist spends \$182.59 per trip on food and beverage. Combined with the projected 36 million visitors this year, food and beverage should serve the local industry \$6.57 billion in revenues from tourists alone.

Casino resorts have been flying in the top chefs and their cooking styles in recent years to tap into that dividend. With gaming revenues last year dropping to 49 percent of the total in southern Nevada and 43 percent on the Strip, food and beverage has risen to become the second largest income source in Las Vegas.

"Food and beverage is not an amenity like it used to be but has become a strategic weapon," says Damian Mogavero, CEO and part owner of Avero Inc., makers of Slingshot software, which monitors and tabulates restaurant activity that can be accessed by restaurant operators through the Internet. "It is a way to differentiate between properties. It encourages guests to visit and it keeps them on the property to gamble. If you look broadly, these hotel and casinos are importing food and beverage to the marketplace. New York City, Chicago, San Francisco and Los Angeles restaurants are expanding there and we're going with our customer base."

National restaurant chains such as Wolfgang Puck, Lettuce Entertain You, B.R Guest, China Grill, and Emeril, among others have been leading the charge into Las Vegas. According to Brian Gordon, principal at local market analysis firm Applied Analysis, typical customers for such high-end eateries fit the consumer profile that can drive up a casino resort's other higher-priced offerings, such as more expensive rooms, spas and shows.

"They are high-value consumers," he says. "That's the right demographic you want to see in Las Vegas."

But the chains are not limiting their sights to the Strip. Mid-range restaurant chains such as Denny's, Olive Garden and Outback are also scouring the valley for locations in order to serve the city's rapidly growing population, currently at about 1.6 million.

"Since this city hit one million people, the competition and vibrancy of the market have taken on a life of their own," says Bob Ansara, president and managing partner of Ricardo's restaurant and board member of the Nevada Restaurant Association. "Chains are good and run better than ever. They are exceptionally well-managed and financed. In the last 15 years, our country by and large has come to like chains. I don't see anything different [in Las Vegas]. Those people are making the biggest splash."

Because of the volume of tourists, high exposure is as much the attraction of the Las Vegas market as raw revenues because it give restaurants the ability to build clientele in markets they have yet to enter. That characteristic, Heffner notes, is compounded by high entertainment value associated with the city itself, allowing companies to be bolder in their innovations without hurting customer expectations.

"See it as the maturing of a company that wants to share cuisine with tourists. If it is an old Napa Valley restaurant, Las Vegas is an exciting way to transcend your offerings. Chicago, New Orleans, San Francisco have the tradition of the old American cities. We are above that league. It stems from the great tourism capital we have become. People are not afraid to try five new concepts here. There are really some kicky things, not just fine dining," he says.

According to Ansara, the growth of national chains is combining with higher real estate prices to put the squeeze on local operators just as the market is hitting fever pitch. "[A restaurant] operator is going to have a hard time factoring real estate costs into operating expenses or menu price," he says. "It doesn't look good for mom and pop establishments. It is increasingly difficult to find a good location and compete against chains. In the near term, it is going to get

tougher for independents before it gets easier ... There will always be a market for the independent restaurateur. But they'll have to work harder, stay closer to the customer and build the business one customer at a time. There won't be a lot of room for sloppiness."

Heffner argues that the local market is still the best opportunity for restaurants, particularly for new businesses, precisely because residential real estate is booming. He cites whole sections of the valley, such as the southeast, south and northwest as being underserved by food establishments.

"Growth areas have not met the need," he says. "There is a limited inventory in housing and restaurants are a couple of years behind. Restaurant choices have lagged behind and I look forward to it leveling out."

The enormous potential is matched, though, by an equal number of risks. Not factoring real estate costs, the initial investment for starting a restaurant here begins at \$500,000 and runs up to \$3.5 million in an industry that has a failure rate of 55-60 percent for new businesses in the first three years, according to an Ohio State University study.

Combined with inconsistent cash flow and high competition from well capitalized chains, the various factors are part of the reason Desert Community Bank typically finances one out of every five to six restaurant projects, according to Troy Morris, the bank's vice president of commercial lending.

"It is a quirky industry," he says. "It is quite challenging to finance. No bank has a large portfolio of restaurant [loans]. Restaurants have fairly high rate of failure. I wouldn't say we scrutinize restaurants more finely but we look at the strengths of the borrower. Banks look to be more secure with restaurant [loans] than other businesses."

Because of the industry's volatility, banks usually back restaurateurs who have experience in the industry and already have accumulated 25-30 percent of the capital required. Even then, creditors will seek to get Small Business Administration guarantees for about 75 to 90 percent of the loan.

In addition, just like any retail business, it's about placing, not timing. "Location is high on list of what we look at," Morris says. "[It is less favorable] if it is next to a Strip property or an area where the demographics are not suitable. I wouldn't put an Italian restaurant at Spring Mountain Road and Arville. It may not be best suited."

He also notes that other aspects peculiar to the Las Vegas market have extra significance. Even if a restaurant is aiming at the local market, so are casinos that have the same large number of restaurants as well as other features such as movie theaters and bowling alleys that make their properties all-inclusive packages.

"Gaming restaurant properties can count on gaming revenues," he says. "In Las Vegas, there is the added dimension of competition you don't see in other parts of the country. The restaurant industry is such a tough market in Las Vegas because it is just part of the entertainment package. Also, in other areas of town, you're not going to get tourist dollars, so you have another dimension. So many factors come into play when considering [an application]."

Nonetheless, local residents seemingly spend as much, if not more, money on dining as those of large metropolitan cities such as New York and Los Angeles. While the warmer climate, low unemployment and 24-hour service all boost the industry, the biggest reason might be that residents have more money to spend.

"What's driving this is an increase in disposable income for individuals," says Gordon. "People aren't earning more but with record low interest rates, they are refinancing, giving them more disposable income or they're pulling out cash from equity."

With the high risk involved, the best way to profit in the restaurant industry is to supply it. By increasing margins 1.5 to 4 points in an industry that averages four percent, Averro doubled sales in 2003 and presently has 400 customers nationwide.

Averro is currently in negotiations with 10 casinos to place their systems across the properties, even though Slingshot has already found a home at some restaurants. Averro believes the local market offers great opportunities. "We hope to expand within Las Vegas and then with some players, expand in all geographical locations in the U.S.," Mogavero says.

It may, however, already be too late to begin in Las Vegas, he adds.