The LIFETIME VALUE of a Player

By Bill Geoghegan

In 1906, Italian economist Vilfredo Pareto observed that 20 percent of the pea pods in his garden contained 80 percent of the peas. That led him to look at other distributions. He calculated that 80 percent of the land in Italy was owned by 20 percent of the population. To his surprise, the same basic distribution of wealth held true in a variety of other countries.

In 1941, Joseph M. Juran, a Romanian-born American management consultant, stumbled across the works of Pareto and began to apply the Pareto principle to quality issues. For example, 80 percent of the problems are caused by 20 percent of the issues. This was also known as "the vital few and the trivial many." While it is questionable that the distribution of exactly 80/20 is always accurate, there is certainly a value in classifying customers, products and quality issues.

Almost all casino operators have player clubs of some sort in which a player accumulates points or is rated for slot play. While table play and poker create their own issues, there is some metric that casino management uses to categorize its players and determine the value of that group of players. Some combination of the following metrics can be used to value a player for a single day or session: buy-in, average bet or bet range, time played, win/loss, game played and location.

The theoretical win for table play=average bet multiplied by time played multiplied by hands/hour multiplied by game edge. For example, a $50 average bet blackjack player playing about four hours per day will, on average, statistically lose about $150 during the gaming session. However, in an environment where a player jumps from table to table and game to game, it is extremely difficult to get any good empirical data on that player. With a packed pit, it takes an extremely sharp pit manager to accurately log a player.

For the slot player, the data gathering is much easier. The theoretical will is simply based on the total money bet or coin in. Players are rewarded for the opportunity they give to the casino, not for wagers lost or won. Here the theoretical win is based on the coin in and the average hold for the game played. If a player moves from game to game, the exact amount of theoretical win can be easily calculated.

Marketing to casino players has traditionally involved an analysis of each player's value and rewarding each player based on his or her perceived value to the casino. Most casinos reinvest about 35 percent to 40 percent of this theoretical win from the customer toward comps for room, food, beverage, shows and airfare reimbursement. Generally speaking, the player's actual win or loss is not a factor when the comp limits are calculated. (Of course, if a player loses a significant amount of money in a very short time, allowances can be made for comps.) In the previous example, the theoretical win of $150 would earn the player about $60 in comps.

In many cases the perceived value of a comp is nowhere near the actual cost of that comp. Shirts, jackets, meals, rooms and other items cost far less to the casino marketing department than the value that the player thinks he or she is getting. Free beverages are a given, with players normally very generous to the servers in gratuities. Players understand that they are more likely to lose than win, but much of their disappointment can be mitigated by receiving something of value for all their losses. The cost of free meals, buffets, show tickets or other items are generally negotiated by the casino at far lower than face value.

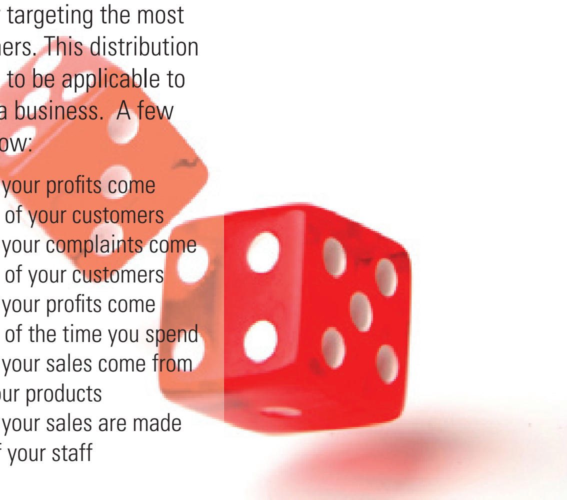
There are a number of challenges in determining how to classify a player. For example, a player that comes to the casino for a weekend once a month and has a theoretical loss of $500 is no more valuable than a local that comes in 20 times a month and has a theoretical loss of $25 per day. Most casinos rate players based on a trip, wherein the per-day play for a short stay is calculated as the basis for comps. The local player, on the other hand, does not require a room or meals, but never shows the same value as the visitor. Those casinos that cater to locals will typically have promotions aimed at enticing the player to visit the casino regularly, by offering free play and gifts.

In order to prioritize the value of a player or player group, casinos determine the true value of a player over a long period of time. Simply put, player lifetime value is the amount by which revenues from a player over time will exceed the casino's costs of attracting, selling and servicing that player. All players are important, but not all players have equal value, and the lifetime of the player may be shortened if that player does not feel adequately rewarded for his or her play.

It may be surprising to note that in general business, most companies find that between 20 percent and 40 percent of customers are not profitable. Often, the most profitable customers

Pareto's Law is widely accepted as a guideline for targeting the most important customers. This distribution is widely claimed to be applicable to many aspects of a business. A few examples are below:

- 80 percent of your profits come from 20 percent of your customers
- 80 percent of your complaints come from 20 percent of your customers
- 80 percent of your profits come from 20 percent of the time you spend
- 80 percent of your sales come from 20 percent of your products
- 80 percent of your sales are made by 20 percent of your staff



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WHERE WERE YOU 20 YEARS AGO?

HOSPITALITY UPGRADE 20TH ANNIVERSARY

Bill Johnson, *Senior Technology Advisor, InterContinental Hotels Group (IHG)*

Twenty years ago I was in Florida working for Johnson Property Hotels at a Holiday Inn, and back then I was on the accounting side of things.

Absolutely. Congratulations!

For more 20th anniversary messages, visit www.hospitalityupgrade.com/20years.

are not the largest customers, but mid-size customers. The smallest customers pay full price and receive less service, but the costs of transacting with small customers may reduce their profitability.

In March of 2001, Andrew MacDonald posted an article called "Dealing with High Rollers" on the Urbino website. This article addressed the severe risk casino operators subject themselves to when they cater to a select few (predominantly Asian) customers playing high-limit Baccarat. McDonald wrote that 14,981,640 hands of Baccarat need to be dealt before the casino can obtain a certain win rate between 1.25 percent and 1.35 percent. This high-win rate volatility, combined with the customer credit risk and high incentives demanded, often make the so-called high rollers a less than attractive proposition for a casino. Thus, the lifetime value of a Baccarat junket may not be as high as most casino executives would have us believe.

Player lifetime value analysis tells us not only which players to aggressively pursue but also hints at the ones to let go.

Speaking on a gaming convention panel some years ago, Bill Hornbuckle – then president of the MGM Grand Resort – observed that it didn't seem logical that a 5,000-room hotel with thousands of slots and table games was dependent on the win or loss results of one "whale" to determine whether the property had a profitable day or not. Be it a particular player segment or an individual player, lifetime value analysis is indispensable for the marketing strategy of a casino. It provides invaluable insights of whom to target and what kinds of relationships to form with each targeted group.

Casinos could factor in the costs and expenses associated with the various market segments (junket players, local high-rollers, interstate players or machine players) and arrive at lifetime value estimates of each segment. Based on the core competencies, risk tolerance and growth objectives, they can then decide which segments to attract and in what priority. A realistic, though more complex calculation would estimate the dollar value of all benefits associated with a loyal customer, not just the long-term revenue stream. The values associated with positive word-of-mouth communication, employee retention and the declining account maintenance costs would then enter into the calculation.

Player lifetime value analysis tells us not only which players to aggressively pursue but also hints at the ones to let go. A casino should not target its services blindly to all players; some segments will be more appropriate and beneficial than others.

An additional challenge is the evaluation of couples or groups that travel together. In most casino club environments, each individual is required to have a separate account. But in many cases, the value of the player is actually the combined value of the group, with costs (especially room comps) that are only singular, but with a gambling budget spread among two or more players.

Rating each individual does not always reflect the true value minus cost over time. Getting the metric wrong can cause a player with long-term value to seek other destinations.

Player clubs have come a long way in recent years toward classifying players, but continue to struggle with lifetime values for finding and keeping their most valued players.

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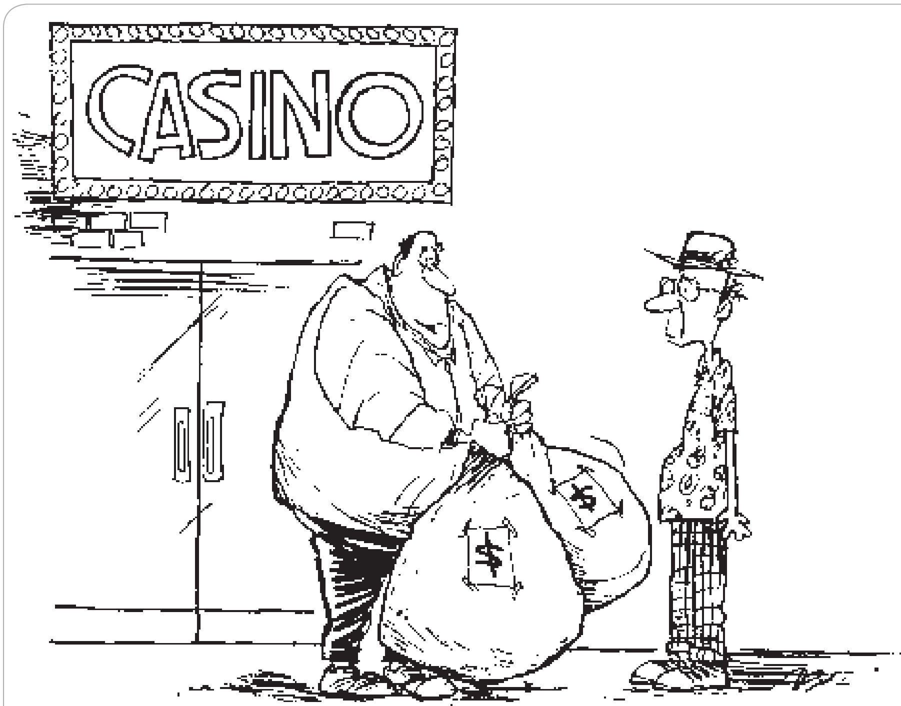

"All I know is I've gotten a lot more perks ever since I started bringing my laundry to the tables."