



# RED ROCK RESORTS: A Second-Class IPO

**Red Rock Resorts/Station Casinos**

**IPO DISSECTED**

A Resource for Prospective Investors

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# Red Rock Resorts: A Second-Class IPO

- Parent company of Station Casinos LLC: operates 19 locals casinos in Las Vegas and 2 tribal casinos.
- Filed for Ch. 11 bankruptcy in 2009 and emerged in 2011.
- 58% owned by affiliate of the Fertitta family.
- 25% owned by Deutsche Bank, a Station lender and one of this IPO's underwriters.



# The Offering: Class A Shares



- \$496–\$571 million in estimated proceeds.
- Red Rock will only own a minority economic interest (33.6%) in Station Casinos.
- 66.4% will be owned by pre-IPO owners.

# Dual-Class Share Structure

| Public Investors                                 | Pre-IPO Owners                                   |
|--|--|
| Class A shares                                   | Class B shares                                   |
| 1:1 voting rights                                | 10:1 voting rights for Fertittas                 |
| 7.3% voting power                                | 92.7% voting power                               |
| 33.6% economic interest in Station Casinos       | 66.4% economic interest in Station Casinos       |
| 15% of tax benefits per Tax Receivable Agreement | 85% of tax benefits per Tax Receivable Agreement |

# Prospective Investors Should Ask:

## About the terms

- Is \$460 million for Fertitta Entertainment excessive?
- Will the Tax Receivable Agreement consume free cash flow?
- How soon after the IPO will Deutsche Bank sell off its significant stake?

## About growth

- How strong is the Las Vegas locals market?
- Why is Red Rock selling hard-to-come-by casino sites in Las Vegas?
- When will Red Rock sign a new tribal gaming agreement?

# High Price for “Internalization”

IPO to fund \$460 million cash payout to Fertitta family-led insiders to internalize management.

| Fertitta Entertainment Purchase Price: | Potential Termination Fee covering 13 of 19 Fertitta Entertainment-managed casinos |
|--|--|
| <b>8.7x</b><br>TTM Management Fees     | <b>1 x</b><br>TTM Management Fees upon 3 <sup>rd</sup> party sale of casinos       |

# Is \$460 million excessive?

|   |               |  |
|---|---------------|--|
| <b>\$460 million =</b>  | <b>93% of</b> | estimated IPO net proceeds of \$495.9 million                    |
|  | <b>20% of</b> | the IPO valuation of Station Casinos' equity at \$2.26 billion   |
|   | <b>8.7x</b>   | Fertitta Entertainment's 2015 management fees of \$52.7 million  |
|   | <b>31x</b>    | Fertitta Entertainment's pro forma 2015 EBITDA of \$14.8 million |

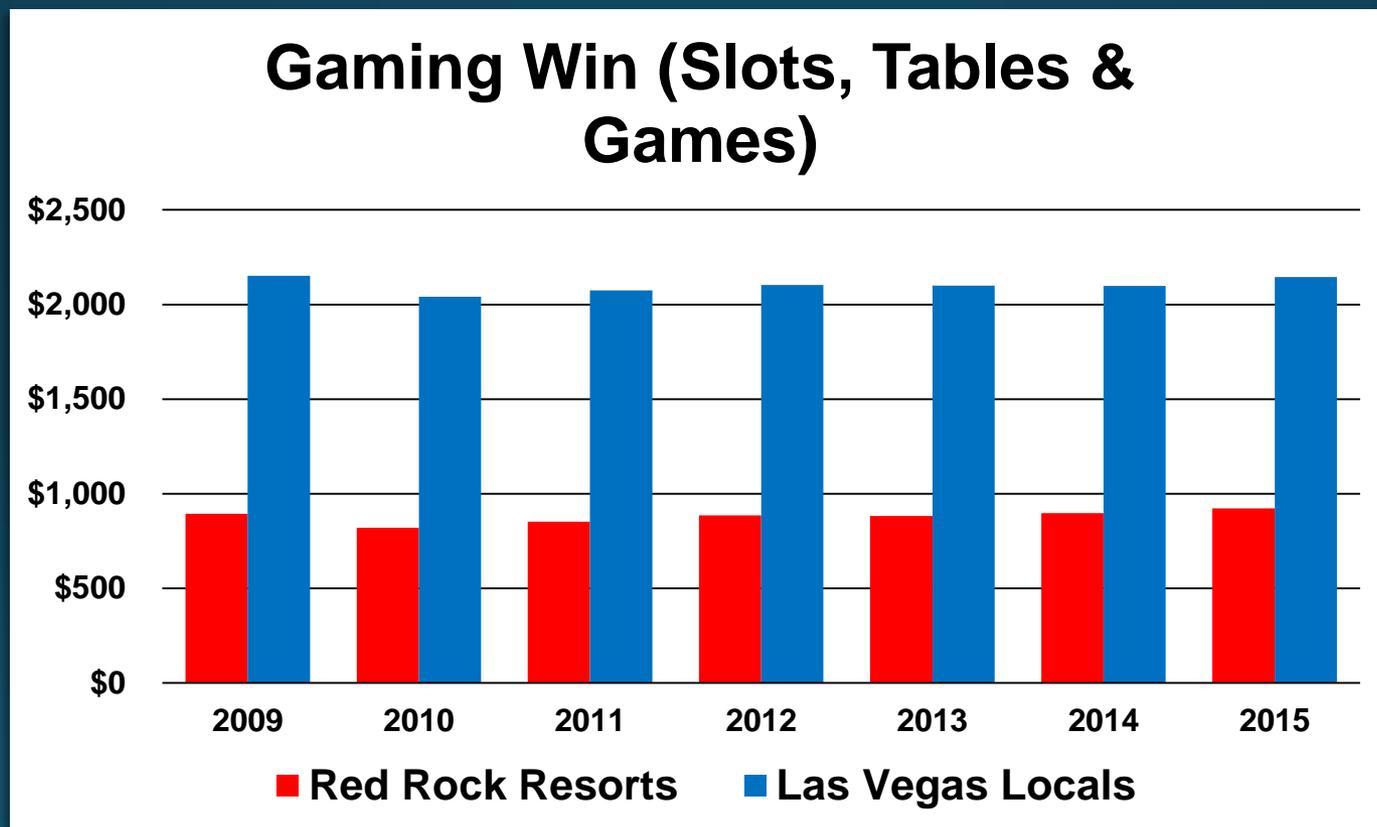
# Rushing to Cash Out?

- Station Casinos attempted a \$300-million dividend recapitalization last spring.
- Station Casinos has paid \$477 million in distributions to its owners from 2013 through April, 2016.
- Fertitta Entertainment borrowed \$30 million to buy a private jet a month before the IPO filing in October. The debt will be paid off as part of the Fertitta Entertainment deal, but the Fertittas will keep the private jet.



# Growth Concerns: Stagnation

Little growth in the company's gaming revenue or its share of Las Vegas Locals gaming market.

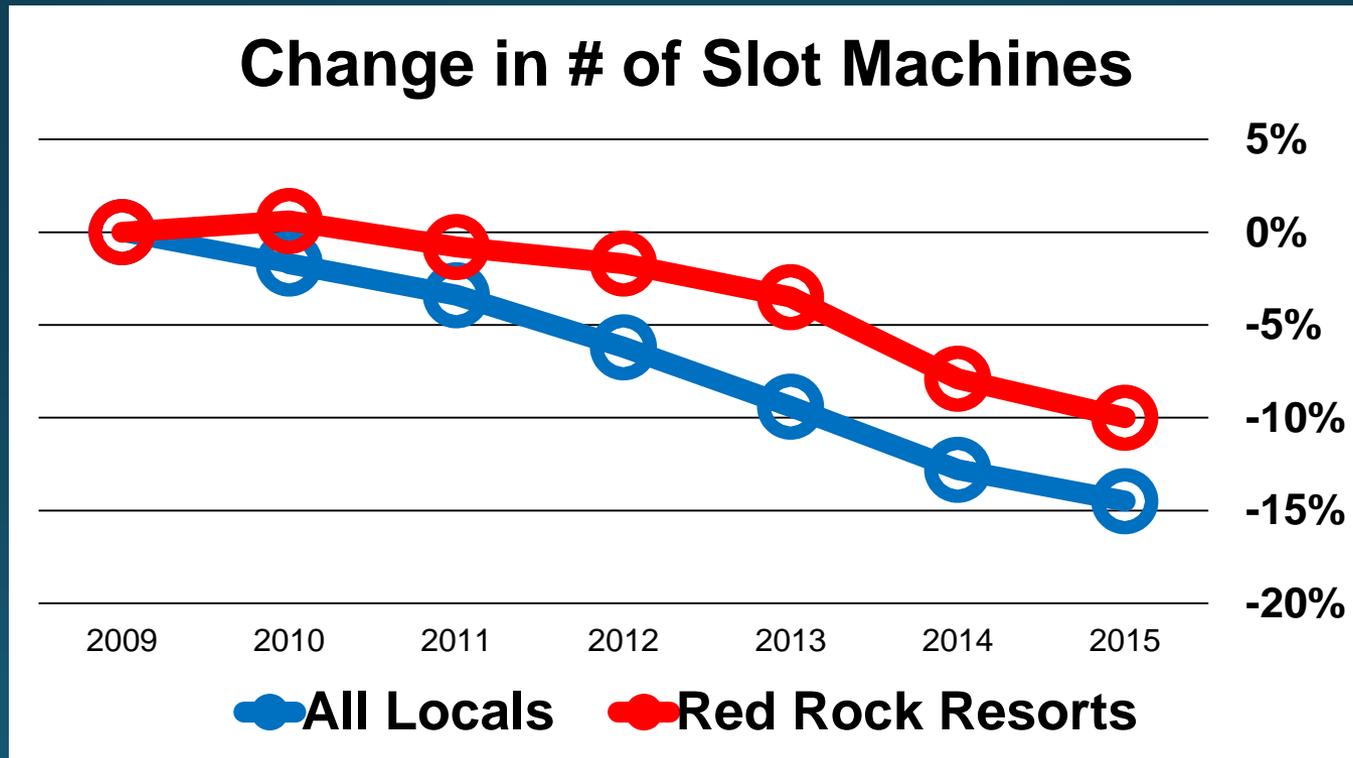


Sources: company filings and Gaming Control Board

# Growth Concerns: Contraction

“A substantial portion of our operating income is generated from our gaming operations, primarily from slot play, which represents approximately 80% to 85% of our casino revenue.” (Red Rock 4/15/16 S-1/A, p. 81)

But, since 2009, there has been a 9.6% decline in the number of slot machines in Red Rock’s 9 major properties.



Sources: company filings and Gaming Control Board

# Growth Concerns: Slow Recovery

According to the National Bureau of Economic Research, there have been two recessions in the past 15 years: one in 2001 and another that ended in June 2009.

Below is a comparison of Las Vegas area growth following these recessions:

## Las Vegas Local Economy

|             | Population ↑ | Average Weekly Wages ↑ | Number of People Employed ↑ |
|-------------|--------------|------------------------|-----------------------------|
| 2002 – 2006 | 22.3%        | 19.2%                  | 24.5%                       |
| 2011 – 2015 | 9.4%         | 3.6%                   | 13.5%                       |

## Las Vegas Locals Gaming Market

| Locals Casinos   | Slot Unit Count | Slot Handle | Slot Handle Ave Monthly Growth |
|------------------|-----------------|-------------|--------------------------------|
| Dec. 2002 – 2006 | ↑18.7%          | ↑36.2%      | \$19.8 million                 |
| Dec. 2011 – 2015 | ↓11.4%          | ↑ 1.1%      | \$0.7 million                  |



# Growth Concerns: Tribal Gaming

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- Tribal gaming management fees =14% of Station Casinos' EBITDA in 2015.
- Significant part of company's EBITDA growth in the past 3 years is from tribal gaming.
- Tribal management agreements expire in 2018 and 2020.
- Last management agreement that expired (in 2010) was not renewed.
- No new tribal casino development or management agreements signed since 2004.

# What's the Growth Plan?

At the Jan. 21 special meeting of the Nevada Gaming Control Board to approve the company's IPO plan, the company confirmed it does not have any concrete development plans.



Member Terry Johnson: “But it doesn't sound as though you have developed anything concrete that you anticipate pursuing as a result of this IPO.”

Richard Haskins, President of Red Rock Resorts: “I think that is exactly right. I think what we are trying to provide for the company, from a growth standpoint, again, whether it is organic or external, is the maximum flexibility and allowing us to be a public company I think provides that.”

# Tax Receivable Agreement

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- Red Rock Resorts will be required to pay 85% of certain tax benefits in cash to pre-IPO owners.
- No cap on the maximum aggregate cash payment.
- Could drain a “substantial” amount of cash and have “material negative effect” on liquidity.
- Fertittas can exercise right to terminate TRA, requiring a lump-sum cash payment to insiders.

Red Rock is required to make TRA payments before making dividend payments.

# TRA Payment Liabilities

TRA payment liabilities commonly increase after IPO and can be as much as 50x EBITDA or 8x IPO proceeds

| Company          | Pre-IPO TRA Estimate | Post-IPO TRA Estimate                    |
|------------------|----------------------|--|
| PBF Energy Inc.  | \$96.8 million       | \$735.4 million<br>(35 months after IPO) |
| Shake Shack Inc. | \$216.1 million      | \$884.6 million<br>(6 months after IPO)  |
| GoDaddy Inc.     | \$1.4 billion        | \$1.7 billion<br>(7 months after IPO)    |

# Deutsche Bank Overhang?

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**Deutsche Bank owns 25% of Station Casinos**

**Deutsche Bank Co-CEO John Cryan:**

“Additionally the wind down of our NCOU positions is matter of high priority. We are making good progress in trying to dispose of Port Elizabeth in New Jersey and also in selling our remaining stake in Station Casinos in Nevada.” (1/28/16)

**Red Rock S-1/A:**

“The market price of our Class A Common Stock could decline due to the large number of shares of Class A Common Stock eligible for future sale upon the exchange of LLC Units by our existing owners.” (4/15/16, p. 44)

# Regulatory Issues

- Deutsche Bank subsidiary pleaded guilty to criminal wire fraud for its role in manipulating LIBOR.
  - Record fines of \$2.5 billion from U.S. and U.K. authorities.
  - Subject of multiple, continuing investigations by federal regulators, including possible money laundering
- Nevada state law ensures that “gaming is free from criminal and corruptive elements.” (NRS 463.0129(1)(b))



“Moreover, if any of our significant stockholders or members of Station Holdco is required to, but does not, apply for a finding of suitability or licensing or is found unsuitable by the Nevada Commission, they may rapidly liquidate their equity holdings, which could cause the market price of our Class A Common Stock to decline.”  
*(Red Rock 4/15/16 S-1/A, p. 47)*

# Do You Want to be a Second-Class Shareholder?

The Fertitta family will have 10:1 voting rights (87% of the combined voting power) with no sunset.



The Fertitta family will control the company and corporate governance, including:

- Election of directors.
- Changes to the company's certificate of incorporation and bylaws.
- The approval of any merger or asset sales.
- Outcome of stockholder actions by written consent or special meeting.
- Transactions with related parties.
- Future issuances of common or preferred stock.

# Poor Corporate Governance Draws Attention of CII

Council for Institutional Investors called Red Rock's corporate governance the "perfect example" for policy statement on newly public companies

## Pending IPO Demonstrates Need for CII Statement

By Rosemary Lally on 3/3/2016 | 0 Comments

Red Rock Resorts, a Las Vegas casino company pursuing an IPO, provides a perfect example of why CII's Policies Committee and board of directors approved a statement (login required) that calls on young companies with corporate governance structures that insulate management from shareholders to sunset these structures within a limited time period.

Red Rock's board approved five antitakeover measures with no sunset mechanisms:

- Dual-class share structure
- Supermajority approval provisions
- Limitations on actions by written consent and special meetings of stockholders
- Fertitta family exemption from a Delaware antitakeover statute
- The board's right to issue preferred stock

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Our website [www.RRRIPOdissected.org](http://www.RRRIPOdissected.org) provides critical analysis of the IPO for prospective investors.

UNITE HERE is a labor union representing 60,000 gaming workers in Las Vegas and 270,000 hotel, gaming, and food service workers in Canada and the United States.

The Culinary Workers Union Local 226, an affiliate of UNITE HERE, is in an ongoing labor dispute with Station Casinos.