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Complimentary rewards in Las Vegas casinos: A literature synthesis and recommendations for profitable complimentary reward programs

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Complimentary Rewards in Las Vegas Casinos:

A Literature Synthesis and Recommendations for Profitable Complimentary Reward Programs

by

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ABSTRACT

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A Literature Synthesis and Recommendations for Profitable Complimentary Reward Programs

by

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This study summarizes academic theories and industry applications related to loyalty marketing schemes, drawing on literature pertaining to casino marketing, behavioral learning theory, loyalty marketing, and economics. Specifically, this study attempts to understand the market conditions and program structure under which Las Vegas Strip casinos may profitably utilize complimentary rewards through increasing short-term revenue and generating long-term loyalty. This literature synthesis provides important professional implications for casino marketers both in terms of effectively designing complimentary reward programs and sustaining profitable business during recessionary times.

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PART ONE

Introduction

During the “Great Recession” of 2007-2009, Las Vegas’ fundamentally shifted its marketing message away from chasing after the luxury visitor, to instead target the “value-oriented” one (Restrepo, 2009). While evidence that customers’ value-proposition has changed can be found in nearly every industry, perhaps no one is more familiar with the impact of its harsh reality than Las Vegas casinos. Between 1995 and 2007, a period that will now be referred to as the “Gilded Age” of gaming, Las Vegas enjoyed undeviating growth, which has all but halted in the following two short years (Restrepo, 2009). During January 2008 and January 2009, Las Vegas Strip gaming revenues plummeted by 9.4%, the largest single-year decline in the city’s history (Green, 2010).

Changing consumer behavior is further evidence that the gaming industry is no longer “recession-proof.” According to the Las Vegas Visitors’ Convention Authority (LVCVA) 2009 Visitor Profile Study, visitor willingness-to-spend on travel and entertainment declined significantly during 2008-2009, in terms of average room rates, food and beverage expenditures, and shopping budgets. However, the most drastic decrease in consumer behavior comes in terms of gaming budgets. Of those Las Vegas visitors who gamble, they had an average gambling budget of \$481.57, down from \$531.98 budgets reported in 2008 and a landslide away from the recent peak of \$651.94 in 2006 (LVCVA, 2009).

Across nearly every media outlet, Las Vegas gaming operators have grieved over how weakening consumer confidence trends have impacted the bottom-line. At a recent casino marketing conference, one executive who expressed, “the casino business today is not about making money, it is about creating value” (Karoul, 2010). This translates to marketers taking

extreme measures to lure back visitors, even at the risk of eroding away profits. Reduced room rates, 2-for-1 meals at high-end restaurants, and more free-play offers, are all examples of the aggressive marketing tactics Las Vegas casinos have resorted to using. Recognizing the new economic reality for many consumers, it is possible to balance consumers' demands for value while still keeping in sight the ultimate goal of making a profit.

Throughout trade publications and academic literature, it is well documented that gaming executives have historically employed casino promotions to increase short-term revenue during off-peak periods and drive long-term brand loyalty (Lucas & Bowen, 2002; Lucas, Dunn, & Singh, 2004; Rose, 2010). The majority of these researchers attest that promotional campaigns have been instrumental in driving foot traffic to Las Vegas (Klebanow, 2007). However, new research suggests that the costs of these promotions outweigh any short-term incremental gains (Lucas & Bowen, 2004). As far as enhancing consumer loyalty, behavioral learning theory suggests that certain promotional rewards may be successful in accomplishing this goal (Rothschild & Gaidis, 1981). On the other hand, economic literature contends that competitive market conditions hinder achieving long-term bonds between the brand and customer (Dowling & Uncles, 1997). Given the inconclusiveness in the literature on the effectiveness of promotions to enhance the casino's value proposition, it becomes clear as to why casino operators may be misguided on how to market "value."

One specific gap in the marketing, economic, and promotional literature is in the area of complimentary rewards. Lowenhar and Russell (1984) support the notion that complimentaries, such as food covers, are related to casino revenues. However, in testing this theory Lucas and Brewer (2001) found that giving away free rooms to premium slot players did not result in incremental revenue from that player. Further, Lucas and Bowen (2004) call for exploratory

research on the effectiveness of promotions to drive incremental revenue and customer loyalty in the service environment. Clearly, while the question of whether loyalty programs actually induce customer loyalty is not a new one, consumer behavior during recessionary times adds another layer of complexity to the issue.

Purpose

The purpose of this paper is to summarize literature pertaining to the historical effectiveness complimentary rewards in casino operations, as well as academic theories related to economics, behavioral learning theory, and loyalty marketing research. Through these frameworks, this study recommends how casino marketers may redesign comp programs to be more successful in generating short-term revenues and long-term loyalty. In addition to discussing loyalty schemes, this study will also discuss issues of pertaining to budgeting marketing activities, stimulating new demand, and customizing rewards to market segments.

Based on gaps in the literature, two questions have been posed: 1) Do complimentary rewards build loyalty, or are they simply a form of price discounting? 2) Are rewarded players profitable investments, or are they only loyal to the offer? These questions frame the underlying limitations of current loyalty rewards, thus the answers will shed light on what modifications are needed to ensure comp programs are a successful casino marketing activity.

Part one of this study introduces why this research is relevant and important to the gaming industry. Part two introduces literature on casino comps, including the definition, history, and current role of comps in casino marketing activities. This section will also review economic, behavioral learning theory, and loyalty marketing research about whether comps fulfill goals as set by management to induce incremental revenue and encourage loyalty. Finally,

part three relates academic theories and market trends introduced in section two, in order to recommend practical solutions.

Problem Exploration

One type of short-term promotion that casino executives have become increasingly reliant on is complimentary rewards (Macomber & Karoul, 2000). Since Las Vegas' inception, executives have offered complimentary rewards, or "comps," to valued players as an incentive to repeat patronage. In their most simple form, comps are a form of price-discounting but are packaged as "free" provisions for food, beverages, and show tickets basis (Marfels, 2010).

As an industry characterized by "look-alike products," comps were originally a means for a casino to differentiate its gaming products from competitors. However, when the Las Vegas gaming market matured, growth slowed, and competition increased, casinos began to escalate the value of complimentary rewards and the frequency with which they are offered in order to compete in this saturated market (Marfels, 2010). As a result, casino marketers have instigated "price wars" by continually reacting to competitors' reward offers by further increasing their own comp expenditures. Perhaps predictably, aggressive comp offers have not been wildly successful in generating short-term profits (Gu, 2008). Furthermore empirical evidence suggests that "follow the leader" tactics may be detrimental on a brand's image in the long-term.

Justification

In this competitive, recessionary market, finding the most profitable and value-added marketing message is of utmost importance to Las Vegas marketers. Many gaming operators presume that because of historical success with using comps to generate gaming revenue, that this strategy will always be lucrative (Lucas & Kilby, 2008). This misconception is based on limited academic research on the subject of casino marketing. Oftentimes, the only information

that is available to casino marketers is anecdotal in nature. Additionally, the success of past marketing tactics may have been obscured by favorable supply-demand conditions. That is, comp rewards simply “worked” because of limited competition for gamblers. Accordingly, there is a need for research addressing when and why comp expenses have outpaced gaming revenue.

Constraints

The limits of this study are inherent to the challenges of any well-executed promotion. In this regard, complimentary services span across a multitude of different departments, each with individual budgets, which challenges measuring aggregate impacts of complimentary expenditures on gaming revenue. For example, promotional expenses for food and beverage departments are calculated separately than slot and rooms departments. Additionally, the majority of gaming companies often do not make such detailed information accessible to the public. Accordingly, this study is limited to focusing on connecting general themes throughout literature and casino operations, which may hinder the applicability at the individual property-level.

PART TWO

Literature Review Introduction

Part two summarizes relevant literature in an attempt to better understand how comp programs may be used to increase short-term profitability and generate long-term loyalty. The literature review is divided into three sections. The first of which describes the evolution and importance of comp programs to the gaming industry, including the role of comp offers in the casino customer's choice process. The second section explores issues related to loyalty marketing, drawing on findings from economics, direct marketing, and behavioral learning theory literature. Within the context of these theories, this section summarizes empirical research on rewarding customers in the airline, retail, leisure services, and casino industries. The third section evaluates comp programs in financial terms in terms of the property-level perspective, as well as aggregate Las Vegas' trends.

Complimentary Reward Basics

Play incentives and promotions have been well-cited by casino executives as crucial components to any casino marketing program (Macomber & Karoul, 2000). The most universally stated goal of comp programs is to increase profit by generating a greater volume of customers than would have otherwise visited in the absence of an incentive. This goal also presents one of the greatest challenges facing casino marketers today: tracking the success of a promotion. While short-term results of a promotion may be quantified in terms of incremental gains in coin-in or foot-traffic, long-term strategies to engender brand loyalty and repeat purchase intentions are often subjective and difficult to measure.

While the underlying goal of comps is clear, the terms of specific programs are subjective to definitions of individual properties and casino executives (McGowan & Brown, 2009).

Despite the term's subjectivity, trade and academic literature have constructed a broad definition of comps based on history and practical applications. According to Rubin (2001), comps are redeemable rebates provided to players on a complimentary basis in order to reward past play or as an incentive for future patronage. Comps can be traced back to the 1930s, when hosts began serving alcoholic drinks at the gaming table, in order to prevent players from leaving the table to take trips to the bar (Hill, 2008). General comps may either be indiscriminate, such as free drinks to anyone on the casino floor or offering free parking, or more hefty price-discounting comps may be based on "if-then" conditions. An example of these conditions can be illustrated by the marketing ploy, "*If* you play our slots between 2 a.m. and 6 a.m., *then* you will receive a free breakfast buffet" (Macomber & Karoul, 2000). Through these programs, the casino can determine the type and value of rewards based on the value of casino play.

Las Vegas is not the only gaming destination that has become increasingly dependent on comp programs. Hill (2008) notes that in Atlantic City, comps have been offered to all levels of players since the 1980s. While comps were traditionally reserved for high rollers, Atlantic City casinos began to offer free rooms, meals, and show tickets to lower-limit gamblers as a means to attract customers during the slow winter months when players faced holiday financial burdens and harsh weather. Within a year, casinos showed positive results: In October 1985, the number of people visiting Atlantic City casinos was 18% higher than October 1984 (McGowan & Brown, 2008). These improvements served as evidence for casino marketers across all gaming markets that comps were in fact a successful form of revenue generation for all segments of players, not only high rollers.

Premium-Player Segment

Premium players have historically been attributed with producing a disproportionately large share of gaming profits (Lucas, Kilby, & Santos, 2002). By rewarding free rooms or meals based on a player's theoretical win, casino executives could compete for the high-rollers and readily justify acquisition costs by the potential revenues associated with this segment (Lucas et al., 2002). This business principle is best described by the 80/20 Law, or the theory that because 80% of revenues are generated by only 20% of a business's customers market efforts should be focused on retaining these elite few (Hill, 2008). Lucas and Kilby (2008) support this notion by through illustrating that comping players does not become profitable until well above \$70 average bet mark. To further illustrate why this is the case, the authors show that at average bets between \$5 and \$25, profit margins are actually negative because of operating expenses. Profit margins rises until the \$50 average bet mark, at which point players become eligible for comps, thus reducing profit-margins. However, because comp expenses are capped by consumption constraints, at an average bet of \$200 per hand, profit-margins recover and continue to rise (Lucas & Kilby, 2008).

However, based on historical trends, it is clear that the complete set of market conditions should be considered when determining the profitability of rewarding premium players. While the inflating value of rewards benefited players, it was detrimental to profits. This is because as competition for the premium-play segment increased, casinos instigated bidding wars with each other by escalating the value of comps (Lucas et al., 2002). Price-based incentives are particularly dangerous in a saturated market in which competitors can simply match reduced prices, thereby removing any short-term advantage. Lucas and Kilby (2008) support this theory through examining table game profit trends between 1996 and 2006. The resources concluded

that that not only have table game profits remained flat, profits in 1996 actually surpassed profits in 2006, which is a clear indication that the costs of incentives are not being filtered down to bottom-line profits (Lucas & Kilby, 2008). For this reason, liberalized comp and discounting policies are attributed to damaging premium-play profits.

Another challenge linked to escalating incentive costs is tracking and issuing rewards to premium-players. Historically, without technology to monitor gaming activity, casino executives would manually track a player's value by estimating average bet, number of hours played, number of decisions per hour, and house advantage (Hill, 2008). Through individual communication between pit bosses, hosts, and players, a discretionary comp-system developed. As the "gate keeper" of comps, casino management often developed an adversary "give-take" relationship with its players.

As noted by Hill (2008) this is often inherent to the challenge of conveying price-incentives to the casino player. Unlike in other leisure settings, such as menus in restaurants or hotel room rates, the "price of casino gaming" is hidden. Instead customers perceive the cost of gaming as a product of what they "won" or "lost" based on their most recent trip alone. To explain this process, Macomber and Karoul (2000) propose that players perceive gaming as a competition with the casino, rather than a purchased entertainment experience. The player has been "trained" by the discretionary comp system to think: "You beat me out of \$1,000, so you owe me ____." In actuality, however, the price of gaming is theoretically derived based on long-term outcomes, as an average of casino win over all trips, regardless of dramatic variances between the best and worst trip. The conflict between the short- and long-term "price" of gaming has been particularly prevalent within the premium-player segment, and given its origins,

it is clear why comps often take on the characteristic of entitlement, rather than a reward in today's gaming environment.

Lucas et al. (2002) explain that price-discounting is also dangerous when casino marketers interpret game outcomes at the individual level. From the operator's perspective, comps may be rewarded to select individuals who "always" lose, based on historical outcomes (Lucas et al., 2002). This philosophy fails to recognize that with games of chance, for every player who always loses, there is a player who almost always wins. When marketers reward comps based on only examining the short-term, individual outcomes, it becomes clear as to why gaming profits have dwindled for the premium-player segment.

Many of these challenges may be traced back to the issues with tracking the premium player's value. Evidence suggests that manually player performances, as observed, tracked, and recorded manually by table game department personnel are often inaccurate (Lucas, 2010). While radio frequency identification (RFID) technology has been expected to revolutionize player tracking accuracy, it does not measure the player's disadvantage on games of skill. Thus, manual tracking remains a hurdle to accurately rewarding premium players.

Even more alarming however, is that players not consistently meeting bet minimums are often not rated at all. In developing a model to predict the profitability of untracked players, Lucas (2010) found that wholesale segment to generate a significant amount of unrated gaming volume. Furthermore, Lucas et al. (2002) note that Las Vegas casinos may be hindering rewarding profitable segments, other than premium players, by obscuring the effects of price-discounting with positive revenue gains in other departments, like room, slot, or entertainment. Again, this highlights the challenges of tracking and measuring all players, premium or otherwise.

Slot-Player Segment

Subsequent to the profitability of the premium-play segment waning, casino marketers recognized the significant revenue contributions from mid- and low-level players (Lucas et al., 2002). For those players who had historically not generated enough play in one trip to earn comps, casino “clubs” were developed through which players could accumulate points from trip to trip (Macomber & Karoul, 2000). Prior to clubs, casino management had little knowledge about a slot player’s wagering volume, which inhibited accurate estimations of player value (Mills, 2007). Without coin-in meters, the only performance data available to operators was drop and win, leading to vast misunderstandings of slot players’ values. Many operators calculated values based on the assumption that all coin sold became drop, and calculated slot hold percentage by dividing win by drop (Lucas & Kilby, 2008). Given the subjective and error-prone valuation process, it is no surprise that executives were hesitant to reward comps to slot players. Additionally, slot players have not traditionally generated substantial revenues to belong to the premium-play segment. As a result, within the discretionary comp system, rewards were generally awarded to slot players who openly asked management for these benefits (Lucas & Kilby, 2008).

This all changed with technological advancements in slot tracking, which enabled players to redeem points for “system-generated comps.” While the first online tracking systems were not without glitches, both casino management and players alike praised the technology for automating the comp process (Rubin, 2001). By collecting and analyzing player data, executives came to the revelation that many valuable slot players had been overlooked and not rewarded by the old discretionary system (Rutherford, 2003; Lucas & Kilby, 2008). Casino executives proposed that increased costs would be compensated for by increased revenues and profits

(Lucas & Kilby, 2008). Just as with the premium-player segment, tracking systems and rewards clubs have actually increased comp costs by opening the comp system to the masses (Lucas & Kilby, 2008). Within the competitive Las Vegas market, a top-tier player may receive as many as 20 direct mail offers within a single month. These offers may include 5-7 point-based comp merchandise gifts (Lucas & Kilby, 2008). In fact, as of 2008, comps issued to slot customers make up the “lion’s share” of overall player reinvestment expenses (Klebanow, 2008).

As for players, slot clubs demystified comp rewards, which had previously been reserved for the premium-play segment (Rutherford, 2003). Players reveled in the fact that even the “average Joe” could “get the comps you want, where you want” (Rutherford, 2003). Harrah’s Entertainment executives explained that this system was explicitly designed to capture “the masses,” or those players without a casino host who previously felt “intimated” by the system (Rutherford, 2003). However, while this technology directly contributed to the slot machine’s popularity, it removed much of the human element that originally made receiving a comp reward so fulfilling (Wakefield & Barnes, 1996). By transforming the process into a “self-service,” research suggests that rewards no longer serve the same benefits as they did in the discretionary form.

Loyalty Marketing Literature

Types of Loyalty Programs

Loyalty programs are offered by retailers, manufacturers, and service providers in order to stimulate short-term profits and long-term loyalty through offering consumers discounts, free goods, cash, or special services (Berman, 2006). Marketers advocate that these programs are profitable for the brand because loyal customers are less price-sensitive, pass on positive recommendations, and are less costly to maintain than acquiring new customers (Dowling &

Uncles, 1997). Despite claimed benefits for both retailers and consumers, it is not empirically clear that rewards programs are effective means of achieving profitability goals. In order to explore these issues, it is beneficial to first examine the success and limitations of loyalty schemes within the industry that pioneered the concept.

Frequent-Flyer Programs

One of the most well-known loyalty schemes is the airline industry's frequent-flyer programs. These programs have been both hailed and criticized in trade press and academic literature for a number of reasons. McGowan and Brown (2009) explain that airlines reward free flights or upgrades after flyers earn a certain number of miles. As a result, there is usually a lag between when the reward is earned and when the benefit is received. Further, flyers often allow points to accumulate, taking advantage of no expiration date. By delaying rewards airlines benefit financially from the time-value of money because, since the programs are funded using revenues from ticket sales at the point of purchase, not when rewards are redeemed (McGowan & Brown, 2008). Berman (2006) cites that frequent-flyer programs help foster customer loyalty, and even proposes that long-term emotional bonds are even more important to profitability than the short-term profitability (Long et. al, 2006). Given these benefits, it is clear why frequent-flyer programs have been praised as imaginative and innovative.

However, it is important to also consider the limitations and shortcomings that the airline industry faced as a result of loyalty programs. It was after the Deregulation Act of 1978, when many airlines struggled to maintain a competitive advantage that American Airlines launched the first frequent-flyer program. The program, cleverly entitled AAdvantage, was presumed to be a game-changer, until only a few weeks later, United Airlines introduced a copy-cat version of its own loyalty program (Berman, 2006). Based on this pattern in the airline industry, it becomes

clear that for a saturated market in which price-promotions can be easily copied, gains from loyalty programs are short-lived.

Casino Loyalty Programs

Through advancements in database marketing and tracking, casinos have advanced traditional loyalty programs through operationalizing player data in order to target rewards at specific consumer segments. Berry (1995) poses that in order for database marketing (DBM) to be successful, marketing activities must include three objectives: 1) attract new players, 2) maintain and enhance existing customer relationships, and 3) recover inactive or defecting customers. In order to know which type of effort should be targeted at which customer, players are segmented by predicated profitability and lifetime value using demographic, psychographic, or performance data (Dowling & Uncles, 1997). Berry (1995) notes the importance of lifetime value of a player, which may be used to differentiate between which customers will only make one purchase in their lifetime, and the other set of customers who will buy from the same organization on a regular basis. Even among lifelong customers, there are players with low-profit margins, while others are not sensitive to price fluctuations.

In order to increase visibility into these segments, casino loyalty programs are often point-based, through which each play-level equates to a certain percentage of tangible incentives, or cash back rewards. Thus, the tiered reward structure is designed to maximize a player's lifelong value by encouraging increased wagers and frequency. Further, by linking membership status to greater rewards received, it is theorized that the tiered structure appeals to human need for achievement (Lucas & Kilby, 2008).

Despite the benefits of tiered-structures, there are limitations, namely that these efforts are focused on only the retention aspect of the three-part framework proposed by Berry (1995).

Further, academic researchers often cite that casinos' DBM efforts are almost always solely focused on maintaining players through monetary benefits (Lucas & Kilby, 2008). Contrary to Berry's (1995) framework, Baier, Ruf, and Chakraborty (2002) pose that database marketing activities should be centered on maintain customers, because in order for a business to "own a customer" marketing efforts should always be targeted at ensuring that a second sale is made. Adding to this research, the "Leaky Bucket Theory" supports retention-focused marketing activities by suggesting that in order for loyalty strategies to be successful, they must be designed to replace the "disloyal" customers who "leak away" with new ones to keep the sales level steady (Dowling & Uncles, 1997). However, the success of this strategy is inherent to the casino's ability to assess whether or not players wish to have a relationship with the casino, which harkens back to Berry's (1995) three-part framework for DBM.

Effectiveness of Complimentary Rewards in Loyalty Programs

Loyalty programs offer a range of rewards, and casinos' complimentary offers are no exception. Marketing literature distinguishes between two types of program rewards: hard and soft attributes (Barlow, 1996). Hard attributes have tangible elements, such as gifts, discounts, or coupons. By contrast, soft rewards offer consumers emotional benefits, such as preferential treatment or personalized communication, which may be simply a note expressing "thank you for your purchase." In other words, hard rewards may be quantified by economical benefits, while soft rewards can only be defined by their emotional components.

While tangible rewards are most commonly featured within casino loyalty programs, the literature is inconclusive about whether soft or hard rewards are more effective in generating long-term loyalty. Barlow (1996) asserts that because the soft-benefits model is less expensive to implement, it can simply be added to the company's existing marketing strategies. However,

this model is more challenging to implement effectively, particularly as consumers begin receiving an increasing number of “thank you” mailers from competitors. For this reason, Barlow (1996) argues for investing in the hard-benefits model, as it will ultimately have huge pay-offs in terms of customer loyalty. Additionally, Kendrick (1998) discovered that consumers who received a tangible gift would be more behaviorally loyal than those who only received only a “thank you” note. On the other hand, Cranage and Mattila (2005) found that without the apology, the gift and discount fell short of appeasing customers after a service failure. Cranage (2009) supported this in finding that gifts may actually decrease customers’ loyalty and attitudes towards the service person, since it removes any sense of leniency the customer may have had towards the service failure.

The challenges to hard rewards may be explained by the behavioral learning theory. The behavioral learning theory, proposes that the type of incentive offered may induce loyalty to the reward, rather than to the brand (Rothschild & Gaidis, 1981). The extent to which a reward is desirable depends on the customer’s commitment level to the product. In this regard, Wirtz, Mattilla, and Lwn (2007) theorized that the importance of reward type is contingent on the type of relationship a customer has with the company. By testing how rewards impact perceived switching costs, the study found that when participants of a loyalty program have low attitudinal loyalty, perceived switching costs will have a positive effect on share of wallet when rewards are present. However, when attitudinal loyalty is high, rewards became less relevant to switching costs. This study illustrates that for low-involvement purchases, rewards may easily replace the purchased product, particularly if the comp reward is beyond the value of the original, purchased product or service. On the other hand, when high-involvement products are accompanied by a small incentive, the product and not the incentive is the primary reward (Dowling & Uncles,

1997). The implications at both ends of the spectrum—high-involvement and low-involvement—should be considered for casino marketers, because gambling may have either one of these characteristics, depending on the person.

Impact of market attributes on complimentary rewards.

As noted previously within the frequent-flyer programs, economic literature proposes that the effectiveness of rewards in creating attitudinal and behavioral bonds to the brand depend on the competitiveness of the market. Macomber and Karoul (2000) pose that in their raw state, complimentaries are a form of price promotion by discounting the gaming product. The price remains the same, but the gaming product is modified to increase the perceived value, which should then serve as a purchase motivator. However, in order for comps to serve as a purchase motivator, the gaming market must be price-elastic, or that the more a casino lowers its “price,” the greater customers will be motivated to purchase the product. On the other hand, in a mature market in which competitors can simply match the new price or incentive, any short-term advantage from lowering the price is removed (Blatteberg et. al, 1995).

As noted in the premium-player segment, price-promotions also present the challenge of convoluting customers’ perception of the “price of gaming” (Macomber & Karoul, 2000). Because of this conflict between the theoretical price of gaming and the short-term actual outcome, complimentaries become an expected part of the player’s gaming experience. Kendrick (1998) argues that service providers are actually responsible for setting this “coupon trap.” Due to market conditions, marketers develop unfounded fears that customers will wait until they receive their next comp to frequent an establishment. Thus, casino operators continuously escalate discount offers in value and frequency (Kendrick, 1998).

Through escalating the frequency and value of competitive offers, players have become loyal to the deal, not the casino. This phenomena is explained by the term “polygamous loyalty,” which Dowling and Uncles (1997) coined to describe those customers who are loyal to a group of providers, instead of one single property. Additionally, Lucas and Kilby (2008) pose that because gamblers are variety seekers, casino marketers cannot expect to capture 100% of a player’s share of wallet. If the rewards of a particular program are viewed to be more attractive than competing programs, it is reasonable to assume membership to one club will not prevent a customer from joining another (Wirtz, et. al, 2008).

The Las Vegas’ gaming market may be defined as a “look-alike” industry, since machines and tables do not differ from casino to casino. Rose (2010) contends that this makes product differentiation is nearly impossible and copy-cat strategies can be readily deployed, and as a result, loyalty programs may be expected to alter short-term behavior, at best (Dowling & Uncles, 1997). For this reason, while comps may serve as a point of differentiation in “look-alike” industries, empirical evidence suggests that long-term purchase intention declines dramatically when comp incentives are no longer offered (Ong, Ho, & Tripp, 1997). Further, as a form of price promotion, comps can be expected to deteriorate brand image, decrease repeat purchases, create entitlement issues, and adversely affect long-term sales and profitability (Kendrick, 1998).

Based on these general loyalty behaviors, loyalty programs are only effective to the extent that they are accompanied by marketing strategies that leverage the brand’s core value proposition, as perceived by the customer. These negative results of these studies could be justified if long-term profitability could be measured in terms of increased visitation. Several studies have tested this by employing survey methods to assess locals’ motivations for visiting

one casino over another. Shoemaker and Zemke (2001) found direct mail was an important driver of repeat patronage among Las Vegas locals. However, the variables of “receive a mailing from the casino” and “types of promotions offered,” held much lower mean values than the attributes “easy drive from where I live” and “you feel safe there” (Shoemaker & Zemke, 2001). Yi and Busser (2008) also looked at Las Vegas local slot players, and found that the top three most influential factors affecting repatronage and willingness to recommend was gaming environment, customer service, and safety. While the researchers found promotions to be positive and statistically significant, the aforementioned top three factors were more important to locals.

Profitability of Complimentary Rewards

The final section of the literature review will examine the profitability of complimentary rewards at three levels: specific rewards, property-specific complimentary and advertising expenses in terms of gaming revenue, and Las Vegas Strip complimentary expenditures in terms of gaming revenue.

Profitability of Specific Complimentary Rewards

Marketing researchers have long questioned the effectiveness of using tangible rewards to build loyalty and generate revenue. Most empirical evidence to date suggests that casino comps generate incremental revenue at the expense of profit. Lucas and Brewer (2001) studied the slot handle associated with premium slot customers who were awarded complimentary hotel room nights. The model found comp hotel rooms did not produce a significant or positive effect on slot handle. Counterintuitive to casino marketers’ intentions, the results challenge the popular expectation that offering free rooms would subsidize a player’s gambling bankroll by alleviating trip expenses (Lucas & Brewer, 2001). With similar results, Lucas and Bowen (2002) found

drawing-based rewards to increase slot volume, however promotional costs did not compensate for the increase. Finally, a number of studies examining direct mail comp offers have found that the costs exceed any increases in slot volume (Lucas & Brewer, 2002; Lucas & Santos, 2003).

Property-Specific Complimentary Expenditures

One way executives analyze the effectiveness of marketing activities is to measure marketing expenditures in terms of incremental revenue generated (Berman, 2006). In casino marketing activities this is the “reinvestment rate” (Lucas & Kilby, 2008). One of the major challenges of measuring the reinvestment rate is that expenses are often scattered throughout nearly every revenue-generating department (Lucas & Kilby, 2008). For example, total comp expenses for one single player may be scattered across the P&L statements of the slot, table game, rooms, beverage, and food departments. Thus, if comp expenses are examined independently measurements may be obscured. As a solution to these issues, the complimentary expense to gaming revenue ratio has become an important benchmarking tool for casino marketers to gauge overall trends in marketing expenditures and to develop a better understanding of player reinvestment efforts (Klebanow, 2007).

McGowan and Brown (2009) examined the strength of the relationship between comp expenses and incremental gaming revenues, actually determined comps to be an effective form of promotion. To study comp programs of five different gaming companies operating in the United States, the researchers used two separate models for each company, one using gross revenue as the dependent variable and the other using only casino revenue as the dependent variable. In both models, the independent variable was promotional allowances, or comp expenses (McGowan & Brown, 2009). In conjunction, advertising expense was also tested for its relationship to revenue. Both models found comp-based promotions to always be correlated

with the dependent variable, and were able to explain a significant portion of its variance (McGowan & Brown, 2009). Additionally, advertising expense was found to be a significant contributor to gross revenue, and even gaming revenue. In this sense, the connection between comp expenditures and advertising expenses should not be overlooked in this study, as it indicates the importance of balancing the two marketing activities in order to reach the most valuable market. The authors call for more research on testing whether the newer, database-marketing comp programs are more effective than the more traditional, discretionary comp programs, in terms of return on investment (McGowan & Brown, 2009).

Las Vegas Trends in Complimentary Expenditures

While the research proposition posed by McGowan & Brown (2009) would be challenging to execute because of the detailed, company-specific information it would require, it is possible to examine this idea at a market-level, through financial data provided by the Nevada Gaming Abstract. This annual report presented by the Nevada Gaming Control Board (NGCB), features financial analysis on all non-restricted gaming licensees producing \$1 million or more in gaming revenues for the previous fiscal year. Among the aggregate financial analysis included in this report is the complimentary expense/gaming revenue ratio. NGCB calculates this ratio by summing all comp expenses for each individual property, across the following seven departments: administration, casino, rooms, food, beverages, and “other” (NGCB, 2009).

Gu (2007) challenges McGowan and Brown’s (2009) evidence that promotional expenses are correlated to revenues, by analyzing NGCB's comp expense/gaming revenue ratio of Las Vegas Strip casinos. The purpose of the author’s study was to recommend the most effective means for Sands Macau Casino to raise gaming revenues, through examining if Macau’s quickly escalating comp and discount expenses mirrors the dangerous path that Las Vegas started on

almost twenty years ago. In 1990, the NGCB reported Las Vegas Strip casinos' comp/gaming revenue ratio to be 9% (NGCB, 1990). However, by 2005 the ratio had more than doubled to 17.8% (NGCB, 2006). Within the same timeline, casino department income for the Las Vegas Strip dropped from 58.2% to 43.8% (NGCB, 1992, 2006). The inverse trend in gaming revenues and comp expenses is indicative that Las Vegas casinos are buying revenue, and paying too much for it (Gu, 2007).

Mirroring this trend, Sands Macau Casino more than double daily gaming revenue in only seven and a half months operation (Gu, 2007). Within the same timeline, Macau's gaming promotional expenses, including comps and discounts, increased at an even faster rate (Gu, 2007). The ratio shows that while in 2004 each dollar of gaming revenues was financed by less than one cent of promotional expense, but by 2005 it had ballooned to 6.5 cents for every dollar of gaming revenue. Based on the similarities between Las Vegas and Macau in terms of the comp expense/gaming revenue, Gu (2007) concludes that comp promotions are the least effective option to raise revenues in Macau.

Complimentary expenses trends from 1999-2009.

Examining how Las Vegas Strip casinos' complimentary expenditures, in relation to gaming revenue, have evolved in the past 10 years, it is possible to further support Gu's (2007) research. In 2009, Las Vegas Strip casinos reported the ratio of complimentary expenses to gaming revenue to be 18.8%, which increased exponentially to 29.5% in 2009 (see Appendix for specific data). The greatest jump occurred between the years 2005 and 2008, during which the NGCB reported ratios of 20.6% and 25.2%, respectively. The increase of 5% in only three years may be attributed to market factors addressed in throughout the literature section. To illustrate, Las Vegas Strip casinos reported a 19.8% comp/revenue ratio in both 2000 and 2001. However,

in 2002, this number jumped a full point to 21%. Similarly, during the years 2006 and 2007, these casinos reported an aggregate 23.8% and 23.6% comp/revenue ratio, respectively.

This pattern is evidence of a few operational defaults, most obviously the “coupon trap” discussed in the literature review. When the ratio is steady, executives perceive the comp as a successful marketing tactic. However this success is shortsighted as customers become trained to only react to promotional offers of a certain value, and become loyal only to whichever casino offers the best deal (Wakefield & Barnes, 1996). As a result, executives become obligated to offering discounts, at a greater value and with heightened frequency. The pattern of drastic jumps in the comp/revenue ratio illustrates the growing sense of entitlement that customers have come to expect comps from Las Vegas casinos.

Boulder Strip complimentary expenses, 1999-2009

The Boulder Strip serves as a point of comparison for Las Vegas Strip expenditures. As noted, during the 1999 to 2009 period, Las Vegas Strip casinos significantly increased comp expenses, while Boulder Strip casinos sustained much less drastic change. Specifically, the Boulder Strip reported comp expenses/gaming revenue to be 12.7% in 1999 and 13.1% in 2009 (see Appendix for specific data). Further, the comp expenses/revenue ratio generally decreased every year from 1999 to 2008, with the exception of 2000 to 2001, when it increased by a slight .2%. Clearly, between the years 2000 and 2008, Boulder Strip casinos were financing much less revenue with comps, than were Las Vegas Strip casinos.

The differences here may be explained by the increasing number and size of firms on the Las Vegas Strip, leading to unchecked growth and competition. As noted previously, by relying heavily on price-based promotions, comps and other forms of monetary benefits served as the only indicator of differentiation between casinos’ “look-alike” products. As economic theory

states, “resources” or customers were allocated to casinos who offered the best prices (Marfels, 2010).

Nevada complimentary expenses, 1999-2009

As predicted by the increased comp expenses on the Boulder Strip and Las Vegas Strip, Nevada’s statewide averages are also escalating. In 1999, the statewide average comp expense/gaming revenue ratio was 16.7%, compared to 24% in 2009 (see Appendix for specific data). While these ratios are below the ratios reported for Las Vegas Strip casinos, these numbers are still significantly higher than those of the Boulder Strip. The escalation of comp expenses statewide demonstrates the impact that system-generated comps had on revenues, specifically during the years 2002-2007, when comp expenses increased from 18.2% to 20%. While database marketing reward systems may be applauded for enabling casino marketers to target rewards, it seems very possible that these systems also cannibalized revenue. The final section will discuss what may be learned from the traditional systems, in order to form recommendations for making the new systems more efficient and profitable.

PART THREE

Professional Implications

Based on the theories and industry applications proposed in the literature section, there are a number implications for casino marketers. This section will begin by extracting “lessons learned” from the discretionary-system traditionally utilized to rewarding premium players, as well as from the airline industry’s frequent-flyer model. These frameworks will then be filtered into a discussion of common pitfalls casino marketers should be aware of when planning reward schemes, accompanied by potential solutions to these limitations.

Lessons Learned

Premium-play segment.

Examining what made the traditional premium-play discretionary-reward-system successful, there are a few lessons that may be applied to the current points-based system. The most underlying issue applies to the “80/20 Law.” While 20% of the casino’s players may have always generated 80% of revenue, it is not clear that executives necessarily rewarded every player in this top-tier. Traditionally, through manually-tracking and maintaining personal relationships, the discretionary-system prevented over-rewarding those players who may have not be loyal, even if they were part of the top 20%. However, with the introduction of the online tracking systems and slot clubs, the “top” tier was automatically identified and rewarded, regardless of customers’ genuine loyalty. The problem with the 80/20 Law is that the “best” 20% are not necessarily always the loyal buyers (Dowling & Uncles, 1997). As polygamous loyalty suggests, heavy buyers will not be exclusively loyal to one brand, but instead will be multi-brand loyal. Given this, it would be beneficial for casino marketers to add “personal discretion” back into the reward system.

Additionally, it was not until competition put upward pressure on incentive expenditures did operators begin to question the profitability of the premium-player segment, and turn to the mid- and low-level players to boost revenues. This may provide foresight to the recent emphasis on marketing Las Vegas' products at a discounted rate to non-gaming visitors. If the previous trend provides any insight, heavily reliance on price-discounting should be terminated in exchange for creating genuine value.

Frequent-flyer programs.

Leading the loyalty marketing movement, American Airlines introduced frequent-flyer programs in order to obtain a competitive advantage in the face of the Airline Deregulation Act of 1978. Only a couple weeks later, American Airlines' main competitor United Airlines, copied the loyalty strategy, thereby minimizing any competitive advantage American Airlines ascertained from its loyalty club. To parallel these trends in the Las Vegas industry, the Corporate Gaming Act of 1969, which enabled corporations to invest capital in casinos, similarly opened the market to competition (Bernhard, Green, & Lucas, 2008). In the years before the corporatization of Las Vegas, this gaming market produced enormous profits, mainly generated by premium players. As the competition for these players increased, so did acquisition costs. However, casino marketers could not comprehend that increasing the value of incentives in the short-term would damage profitability in the long-term.

As demonstrated by the airline industry, in mature, saturated markets loyalty programs offer similar membership provisions, purchase requirements, and rewards as competitors. Just as American Airlines failed to anticipate how easy it would for United Airlines to copy its reward scheme, Las Vegas marketers are failing to see how easy price-discounting can be copied. This applies to not only competing for the premium-play segment, but also to slot clubs. For example,

while a member can earn five points for every dollar spent at one casino, its competitor may gain a competitive advantage by offering the same rewards at two points per dollar (Berman, 2006). On the other hand, the airline industry also demonstrates that without transparent redemption structures and customized rewards, customers may perceive loyalty programs as simply qualification barriers to complimentary rewards, and become disinterested in redeeming points. Revising the currency and tier structure may alleviate these challenges.

Potential Pitfalls of Complimentary Rewards

In order to tackle redesigning the loyalty program, marketers should first be aware of potential pitfalls. To summarize the literature review and lessons learned, limitations of Las Vegas complimentaries programs include: 1) competitive considerations within a saturated market; 2) not properly using rewards to channel demand; 3) expending more money on incentives than the profits expected in return.

Copy-Cat Reward Schemes

Loyalty is defined by a customer's set of choices, thus a casino's value must be relatively greater than the value offered by the competitive set (Lucas, Dunn, & Singh, 2005). It is clear that with price-discounting, competitors may easily counter price-discounting by offering the "greater" reward. To illustrate, if a competitor's price cut is considered more valuable than another property's, customers will be more motivated by an immediate reward, than the promise of a delayed one. The self-deprecating effects of price-wars that have become common-place in the Las Vegas' market may be best summarized by a Fortune 500 CEO who said, "[a]s long as your competitors are doing it, you have to [have a guest loyalty program.] If we all stopped doing it I wonder what the results would be." (Berman, 2006).

While price-discounting strategies are the most convenient means to reward players, they are no longer effective in saturated markets, and instead marketers should look towards implement non-price rewards. As noted, complimentaries create value in two ways, by either offering “more” for the same price, or reducing the price without changing the product. In these instances, the real or perceived increase in value becomes the motivator. While rewards in the form of “adding more” is often underutilized, they are less susceptible to copy-cat strategies, and can be a more effective means to generate incremental profits and loyalty. In order for reward programs to serve as a differentiator, the value proposition must be truly unique. As noted, soft rewards play a crucial component to ensuring rewards are effective, and are also the most difficult to imitate. Soft rewards may be integrated into tangible rewards through service, quality, or even entertainment. For example, if a casino’s value proposition is service, the complimentary reward should align with that by offering additional, personalized host services, or faster hotel check-in times.

Demand Management

In order for comp programs to serve as motivators, rewards must be aligned with either stimulating the demand of existing customers or players, or stimulating demand among consumers who would not otherwise patronize the casino (Macomber & Karoul, 2000). These two concepts may be defined as outward and inward marketing strategies.

Outward marketing strategies.

Loyalty rewards schemes are typically designed to reward past play, however comp offers that are designed to incentive future play may be a more profitable strategy. Again, the success of these rewards to incentivize customers depends on whether the reward directly supports the value proposition of gaming experience, thereby differentiating the product.

Oftentimes Las Vegas casinos' reward schemes are designed to motivate customers in an indirect route by rewarding complimentary gifts that are inconsistent with the positioning of the target product. For example, Las Vegas casinos' loyal players may be rewarded with a range of gifts from small kitchen appliances to golf trips. On the lower-end of the spectrum, these rewards fail to instill aspirational value, and on the high-end these comps are often out of proportion to the amount spent (Dowling & Uncles, 1997). Behavioral learning theory supports that rewards directly linked to the value proposition of the brand will increase the program's success by bonding customers to the brand, and not the rewards (Rothschild & Gaidis, 1981).

By aligning the casino's products with what current visitors need or want, outward marketing is the most direct means to generate revenue markets. Focusing on its existing customer base, casino marketers select a property objective, and then determine what the value-proposition should be in order to achieve this objective (Macomber & Karoul, 2000). For example, one casino's objective may be to increase midweek slot-play among seniors, and accomplishes this through offering charter bus program catering to senior residential communities. While this is not the most exciting complimentary service, it extracts demand from a segment with an existing "raw desire" to purchase the product, by removing the utility issue—transportation—that stood in the way of the senior customer-base. Here, the value-proposition does not need to be a price-reduction, but instead is *adding* something to the existing gaming product, thereby offering "more" for the same price.

Inward marketing strategies.

Alternatively, rewards may strengthen brand equity through simply growing market share to capitalize on unmet demand. In short, current casino complimentaries should utilize rewards to maximize motivation of the most profitable customer, by serving as an impetus for a casino visit

among players. In order for rewards to fulfill that role, they must be customized to the individual. While database marketing is vital to identifying who the casino's loyal customers are, it should be kept in mind that those customers active in the database are unlikely to be representative of all *potential* customers (Dowling & Uncles, 1997). Considering this, current reward schemes may be ineffective at appealing to new and under-penetrated market segments.

As noted earlier, there is a positive relationship between distribution coverage and market share (Dowling & Uncles, 1997). Rewards may be used to market "inward," by identifying under-penetrated and new markets, determining which types of rewards would best motivate these segments, and then tailoring rewards to extract this unmet demand. While Las Vegas casinos are currently using this structure to build pricing-discounts around non-gaming amenities, there is still room to grow.

One way to determine which types of rewards will motivate unknown segments is to increase distribution outlets. Part of getting the "right message, to the right customer, at the right time" is finding the "right" delivery vehicle to get the message to the intended audience. There are a vast number of delivery vehicles, including: signage (billboard and outdoor advertising), print (newspapers, mailed circulars), radio, television, direct mail, telemarketing and Internet (Macomber & Karoul, 2000). Again, because casino marketers tend to blindly follow-suit of competitors, many of these channels are not maximized. In order to accomplish this, trial programs should be executed regularly to test, track, and measure saturation levels within new segments. In the Las Vegas market where competitors are always trying to "out-shout" the other with marketing messages, as trial programs illuminate under-penetrated markets without investing the substantial cash necessary for a full-blown campaign.

Effectively Budgeting Complimentary Rewards

While not specifically addressed in the literature review, escalating costs of complimentary rewards should clearly indicate the need for better budgeting. Oftentimes, marketers do not perform a complete a customer cost-benefit analysis when issuing rewards due to the challenges of summing costs across departments. When budgeting does occur, programs budgets rarely include actual figures, and instead reflect guesses and estimates (Macomber & Karoul, 2000). However, without sound budgeting, complimentary rewards will inevitably fail. This is because budgets should be the basis of goals, and without sound goals, it is impossible to determine whether a marketing objective was successful or not. Setting budgets reflecting both actual and projected numbers will facilitate marketers in creating sustainable, profitable complimentary programs.

Conclusion

Casino marketers rarely engage in activities to retain customers other than price discounting. This narrow-minded strategy has several implications, as indicated in this study. As players ascend players' club tiers, comps become an increasingly costly liability. Further, technology enabling casinos to customize and differentiate comp services for loyal customers can also be costly and operationally challenging to implement. Many casino marketing activities have been "borrowed" from other industries, including rewards clubs. However, based on the literature review, it becomes clear that casinos sell a unique combination of product and service, which should be reflected throughout its marketing strategy.

To reiterate the statement expressed at the beginning of this study, "casino business is not about making money...it is about creating value" (Macomber & Karoul, 2008). While the economic slowdown may be challenging for gaming operators, executives should remember that

the goal of business is to generate profits. Thus, the crucial question remains: Are the tangible rewards offered to loyalty customers more profitable than any of the alternatives? The answer must be rooted in customers' perceptions of whether the reward supports the value proposition of the casino's product and services. Based on these professional implications, there are means through which Las Vegas casinos can utilize rewards to enhance the value proposition by either better aligning their product with the needs and expectations of the marketplace, or stimulate new demand that did not previously exist.

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Appendix

Geographic Variance of Comp/Revenue Ratios: General Trends

| Geographic Area/ Year | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|------------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Las Vegas Strip | 18.8 | 19.8 | 19.8 | 21 | 20 | 20.5 | 20.6 | 23.8 | 23.6 | 25.2 | 29.5 |
| Boulder Strip | 12.7 | 12.2 | 12.4 | 11.4 | 11.8 | 10.9 | 10.6 | 10.7 | 11.5 | 11.7 | 13.1 |
| Nevada | 16.7 | 17.2 | 17.3 | 18.2 | 17.9 | 18.3 | 18.2 | 19.6 | 20 | 21.3 | 24 |

Note. Adapted from “Nevada Gaming Abstract,” by Nevada Gaming Control Board, 1999-2009.

