THE WALL STREET
THE JOURNAL REPORT: ECONOMIC ROUNDUP

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Bad Odds

As more states look to win the economic jackpot with casinos, evidence suggests they are playing a losing hand

Out on the Great Plains, an experiment is under way: Under a new state law legalizing gambling, Kansas City, Kan., could soon be lit up by the first full-blown casino resort in its 135-year history.

If the plans come to fruition, Kansas will be the 13th U.S. state to bet that commercial casinos will prove to be a win-win game, reaping profits for the casino owners and boosting development for their hosts at the same time. "We'll see a big economic benefit," Kansas Gov. Kathleen Sebelius said when she signed the enabling legislation in April.

A growing body of research and experience, however, suggests the odds are not stacked in the state's favor. Some economists go so far as to call casinos a sort of global zero-sum game, in which the outcome for a host city depends on the casino's ability to attract out-of-state tourists and separate them from their money -- a feat that becomes increasingly hard to achieve as more states install casinos of their own.

"There are two simple questions: Where does the money come from, and where does the money go?" says William Thomson, a professor of public administration at the University of Nevada in Las Vegas. "If the customers live in the local area, there's no way you can have economic development."

No place in the U.S. has been more successful at attracting out-of-town money than Las Vegas, which hosts nearly 40 million visitors a year. Prof. Thomson estimates that those visitors contribute more than four-fifths of the area's annual gaming revenues, which exceed $8 billion.

Taking a Shot

Over the past few decades, more and more regions of the U.S. have decided to take a shot at doing what Las Vegas has done. According to the American Gaming Association, 12 states now have operating commercial casinos, up from only two in 1987 (that doesn't include racetrack casinos and casinos run by Indian tribes). Consumer spending on commercial casino gaming stood at $32.42 billion in 2006, up from $17.1 billion a decade earlier and more than triple the level of U.S. movie box-office sales.

States and municipalities typically count the benefits of casinos in terms of jobs and tax revenues. In 2006, commercial casinos employed about 366,000 people and paid about $5.2 billion in direct gaming taxes, according to the American Gaming Association.

More blackjack dealers and gaming taxes, though, don't necessarily add up to growth in economic well-being. For one, casinos often take business from other entertainment venues, such as theaters or sports bars. As a result, some economists -- such as Earl Grinols, a former senior economist on the president's Council of Economic Advisers who now teaches at Baylor University in Texas -- contend that, on average, casinos actually make no net tax contribution. The effect on jobs could actually be negative, because many modern casinos -- replete with slots and video-poker machines -- need fewer employees per customer than the businesses they tend to replace.

"The problem with cities is that they only look at the positive side," says Ricardo Gazel, who is an economist at the Washington, D.C.-based Inter-American Development Bank, and who authored a paper on casinos and economic development while at the Federal Reserve Bank of Kansas City. "They look at revenues and the creation of jobs, but they don't look at the destruction of other jobs."

What Benefit?

Also, casinos don't necessarily provide the same benefits that most other businesses do. If, for example, a city or state attracts software or biotech firms, the community is likely to benefit not only from job creation,

but from the services or products that these types of companies provide. In the case of software, that "utility" is added productivity or entertainment for anyone who uses the product. For biotech, it can be health benefits.

The utility of casino gambling, however, is harder to pin down. Proponents say casinos provide the thrill of risk-taking, along with drinks, music and lights. "A casino is just like a widget factory or a newspaper," in that it produces something of value, says Eugene Christiansen of Christiansen Capital Advisors, a consultancy that counts governments and gaming companies among its clients.

Some economists, though, doubt the excitement of casino gambling is worth what people pay for it. In Las Vegas, for example, the average visitor who gambles spends -- meaning loses -- about $650. Many people aren't shelling out that money purely for entertainment: Prof. Grinols, citing various studies, estimates problem and pathological gamblers, on average, account for as much as half of casinos' gaming revenues. That suggests that to a large extent, casinos do little more than transfer money from one group of people to another -- in this case, from their customers to their investors and employees. "With a service like gambling you don't have that mutual value of trade," says Prof. Thomson.

Losing Bets

Beyond that, studies have shown that casino gambling imposes significant costs on communities. The most important is crime: Cities with casinos provide relatively attractive targets for criminals, who see opportunities in the crowds of people carrying large amounts of cash. In a study of more than 3,000 U.S. counties published last year in the Review of Economics and Statistics, Prof. Grinols and economist David Mustard at the University of Georgia estimated that, on average, about 8% of crime in casino counties was attributable to the casinos. Taking all the costs and benefits of casinos into account, Prof. Grinols has concluded that the introduction of a casino ultimately incurs an average net cost of at least $97 per resident per year.

A few communities, such as Las Vegas, and to a lesser extent smaller gambling centers like Biloxi, Miss., come out ahead because they also are successful as tourist destinations, drawing most of their gamblers from afar. That keeps the benefits at home and distributes the costs elsewhere, because people take their losses and problems back to the places from whence they came. "Because they're drawing such huge volumes of money from other areas, you can argue that's enough to outweigh the local negatives," says Prof. Grinols. "You're imposing the social costs on some other place."

But with more and more places trying to become the next Las Vegas, the greater competition lowers the chances that any will succeed. A city aiming to install a casino "is very unlikely to become anything more than a regional player, and its major customers are likely to become its own residents," says Bill Eadington, a professor of economics at the University of Nevada in Reno.

The pitfalls are evident in places like Gary, Ind., and Detroit, which both introduced casino gambling in the hopes of stimulating moribund local economies. The three casinos in Detroit, built in part to compete with casinos across the border in Canada, cater largely to a local clientele, says Fred Wacker, an avid gambler and professor of interdisciplinary studies at Wayne State University in the city. Revenue from the three casinos has grown steadily, and they contributed about $158 million in gaming taxes to the state budget in 2006. But Prof. Wacker, who initially favored bringing in casinos, sees little positive impact on the area.

"Casinos always make money, but how much good they're doing for Detroit's economy is another question completely," he says. "I don't see much community development."

Even when casinos do manage to attract gamblers from out of town, they can spur neighboring regions to retaliate, which is one explanation for the growing number of states taking the plunge. In Kansas, for example, the bid to bring in casinos is partly an attempt to get some business back from neighboring Missouri, which has casino boats on the Missouri River in Kansas City, Mo. "In those parking lots it's like 40% to 50% Kansas tags on the cars," says Ed Van Petten, executive director of the Kansas Lottery, which oversees gambling operations in the state. "Hopefully it would stop a money drain of Kansas dollars going to Missouri businesses."

Proponents of gambling on the Kansas side of Kansas City also believe it will help create the critical mass needed to make the area a major tourist attraction. Judging from the experience of other places, the city might do well to limit its wager. "Gambling can address small issues," says Prof. Eadington. "It cannot address big issues in a positive way."

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