MANDALAY RESORT GROUP
Form 10-Q
June 14, 2002

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SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

ý **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended April 30, 2002

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____________ to _____________

Commission file number 1-8570

MANDALAY RESORT GROUP

(Exact name of registrant as specified in its charter)

Nevada	**88-0121916**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)

3950 Las Vegas Boulevard South, Las Vegas, Nevada 89119
(Address of principal executive offices)

(702) 632-6700
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at May 31, 2002

Common Stock, $.01 2/3 par value	**68,395,157 shares**

MANDALAY RESORT GROUP AND SUBSIDIARIES

Form 10-Q

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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

MANDALAY RESORT GROUP AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)
(Unaudited)

	April 30, 2002	January 31, 2002
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 121,088	$ 105,905
Receivables	63,213	76,461
Inventories	29,056	30,555

	April 30, 2002	January 31, 2002
Prepaid expenses and other	48,528	54,066
Total current assets	261,885	266,987
PROPERTY, EQUIPMENT AND LEASEHOLD INTERESTS, at cost, less accumulated depreciation and amortization of $1,201,860 and $1,162,203, respectively	3,063,175	3,049,812
EXCESS OF PURCHASE PRICE OVER FAIR MARKET VALUE OF NET ASSETS ACQUIRED, NET	43,549	45,445
INVESTMENTS IN UNCONSOLIDATED AFFILIATES	529,802	554,086
OTHER INVESTMENTS	47,628	35,751
DEFERRED CHARGES AND OTHER ASSETS	83,731	84,953
Total Assets	$ 4,029,770	$ 4,037,034

LIABILITIES AND STOCKHOLDERS' EQUITY

	April 30, 2002	January 31, 2002
CURRENT LIABILITIES:		
Current portion of long-term debt	$ 36,251	$ 39,251
Accounts payable trade	44,489	33,473
Accounts payable construction	12,758	8,284
Accrued liabilities	243,115	228,233
Total current liabilities	336,613	309,241
LONG-TERM DEBT	2,387,084	2,482,087
DEFERRED INCOME TAX	200,415	199,478
OTHER LONG-TERM LIABILITIES	105,215	109,258
Total liabilities	3,029,327	3,100,064
MINORITY INTEREST	2,727	(3,639)
STOCKHOLDERS' EQUITY:		
Common stock, $.01 $^{2}/_{3}$ par value Authorized 450,000,000 shares Issued 113,634,013 shares	1,894	1,894
Preferred stock, $.01 par value Authorized 75,000,000 shares		
Additional paid-in capital	570,620	572,992
Retained earnings	1,423,234	1,374,376
Accumulated other comprehensive loss	(18,693)	(21,902)
Treasury stock (45,268,090 and 45,278,193 shares), at cost	(979,339)	(986,751)
Total stockholders' equity	997,716	940,609
Total Liabilities and Stockholders' Equity	$ 4,029,770	$ 4,037,034

	April 30, 2002	January 31, 2002

The accompanying notes are an integral part of these condensed consolidated financial statements.

MANDALAY RESORT GROUP AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except share data)
(Unaudited)

	Three Months Ended April 30,	
	2002	**2001**
REVENUES:		
Casino	$ 308,318	$ 318,678
Rooms	155,408	170,800
Food and beverage	106,745	109,273
Other	80,760	82,036
Earnings of unconsolidated affiliates	30,569	31,245
	681,800	712,032
Less-complimentary allowances	(43,659)	(42,951)
	638,141	669,081
COSTS AND EXPENSES:		
Casino	158,153	170,297
Rooms	50,130	52,481
Food and beverage	70,560	75,288
Other operating expenses	49,438	56,728
General and administrative	100,484	106,654
Corporate general and administrative	8,373	4,849
Depreciation and amortization	41,015	54,970
Operating lease rent	12,925	9,710
Preopening expenses	469	
	491,547	530,977
INCOME FROM OPERATIONS	146,594	138,104
OTHER INCOME (EXPENSE):		
Interest, dividend and other income	2,518	387
Guarantee fees from unconsolidated affiliate	193	584
Interest expense	(56,158)	(54,475)
Interest expense from unconsolidated affiliates	(2,127)	(2,748)

	Three Months Ended April 30,	
	(55,574)	(56,252)
MINORITY INTEREST	(11,578)	(6,757)
INCOME BEFORE PROVISION FOR INCOME TAX AND CUMULATIVE EFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE	79,442	75,095
Provision for income tax	28,722	27,733
INCOME BEFORE CUMULATIVE EFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE	50,720	47,362
Cumulative effect of a change in accounting principle for goodwill	(1,862)	
NET INCOME	$ 48,858	$ 47,362
BASIC EARNINGS PER SHARE		
Income before cumulative effect of change in accounting principle	$ .74	$ .62
Cumulative effect of a change in accounting principle	(.03)	
Net income per share	$ .71	$ .62
DILUTED EARNINGS PER SHARE		
Income before cumulative effect of change in accounting principle	$ .71	$ .61
Cumulative effect of a change in accounting principle	(.03)	
Net income per share	$ .68	$ .61
Average shares outstanding basic	68,487,942	76,111,308
Average shares outstanding diluted	71,345,845	77,487,220

The accompanying notes are an integral part of these condensed consolidated financial statements.

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MANDALAY RESORT GROUP AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended April 30,	
	2002	**2001**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 48,858	$ 47,362
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	41,015	54,970
Provision for bad debts	3,522	7,177
Decrease in deferred income tax	(790)	(1,347)

	Three Months Ended April 30,	
Increase (decrease) in interest payable	2,779	(2,425)
Increase in accrued pension cost	2,113	1,367
Gain (loss) on disposition of fixed assets	(52)	577
Impairment loss	1,862	
(Increase) decrease in other current assets	16,763	(4,539)
Increase in other current liabilities	23,119	43,397
Decrease in other noncurrent assets	1,583	390
Unconsolidated affiliates' distributions in excess of earnings	24,180	1,836
Minority interest in earnings, net of distributions	6,366	4,022
Other	(761)	
Total adjustments	121,699	105,425
Net cash provided by operating activities	170,557	152,787
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(54,593)	(23,215)
Increase (decrease) in construction payable	4,474	(2,133)
Increase in other investments	(10,850)	(10,852)
Other	454	617
Net cash used in investing activities	(60,515)	(35,583)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net effect on cash of issuances and payments of debt with original maturities of three months or less	(80,000)	(20,000)
Principal payments of debt with original maturities in excess of three months	(18,099)	(14,105)
Exercise of stock options	8,404	1,285
Purchases of treasury stock	(2,914)	(17,406)
Other	(2,250)	(3,076)
Net cash used in financing activities	(94,859)	(53,302)
Net increase in cash and cash equivalents	15,183	63,902
Cash and cash equivalents at beginning of period	105,905	105,941
Cash and cash equivalents at end of period	$ 121,088	$ 169,843
SUPPLEMENTAL CASH FLOW DISCLOSURES		
Cash paid during the period for:		
Interest (net of amount capitalized)	$ 51,493	$ 55,369
Income tax	$ 215	$ 2,917
Noncash items:		
Increase (decrease) in market value of interest rate swaps	$ 4,670	$ (15,972)
Increase in market value of investment in insurance contracts	$ 1,027	$

The accompanying notes are an integral part of these condensed consolidated financial statements.

MANDALAY RESORT GROUP AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(All information for the three months ended April 30, 2002 and 2001 is unaudited.)

Note 1. Summary of significant accounting policies

Principles of Consolidation and Basis of Presentation

Mandalay Resort Group (the "Company"), which changed its name from Circus Circus Enterprises, Inc. effective June 18, 1999, was incorporated February 27, 1974 in Nevada. The Company owns and operates hotel and casino facilities in Las Vegas, Reno, Laughlin, Jean and Henderson, Nevada and a hotel and dockside casino in Tunica County, Mississippi. In Detroit, Michigan, the Company is the majority investor in a temporary casino which opened December 14, 1999. It is also an investor in several unconsolidated affiliates, with operations that include a riverboat casino in Elgin, Illinois, a hotel/casino in Reno, Nevada and a hotel/casino on the Las Vegas Strip. (See Note 3 Investments in Unconsolidated Affiliates.)

The consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries and the Detroit joint venture (53.5% owned), which is required to be consolidated. Material intercompany accounts and transactions have been eliminated. Investments in 50% or less owned affiliated companies are accounted for under the equity method.

Minority interest, as reflected on the condensed consolidated financial statements, represents the 46.5% interest of the minority partners in MotorCity Casino in Detroit, Michigan.

The condensed consolidated financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading. In the opinion of management, all adjustments (which include normal recurring adjustments) necessary for a fair statement of results for the interim periods have been made. The results for the three months are not necessarily indicative of results to be expected for the full fiscal year.

Certain reclassifications have been made to the financial statements for the three months ended April 30, 2001 to conform to the financial statement presentation for the three months ended April 30, 2002. These reclassifications have no effect on net income.

These condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended January 31, 2002.

Earnings Per Share

Basic earnings per share is computed by dividing net income by the weighted average number of common shares outstanding during the period, while diluted earnings per share reflects the impact of additional dilution for all potentially dilutive securities, such as stock options.

The table below reconciles weighted average shares outstanding used to calculate basic earnings per share with the weighted average shares outstanding used to calculate diluted earnings per share. There were no reconciling items for net income.

	Three Months Ended April 30,	
	2002	**2001**

	Three Months Ended April 30,	
	(in thousands, except per share data)	
Net income	$ 48,858	$ 47,362
Weighted average shares outstanding (basic earnings per share)	68,488	76,111
Stock options	2,858	1,376
Weighted average shares outstanding (diluted earnings per share)	71,346	77,487
Basic earnings per share	$ .71	$ .62
Diluted earnings per share	$ .68	$ .61

Comprehensive Income

Comprehensive income is a broad concept of an enterprise's financial performance that includes all changes in equity during a period that arise from transactions and economic events from nonowner sources. Comprehensive income is net income plus "other comprehensive income," which consists of revenues, expenses, gains and losses that do not affect net income under Generally Accepted Accounting Principles. Other comprehensive income for the Company includes adjustments for minimum pension liability and adjustments to interest rate swaps, net of tax.

Comprehensive income consists of the following (in thousands):

	Three Months Ended April 30,	
	2002	2001
Net income	$ 48,858	$ 47,362
Cumulative effect of a change in accounting principle for interest rate swaps		(9,300)
Change in fair value of interest rate swaps	3,209	(1,498)
Comprehensive income	$ 52,067	$ 36,564

The accumulated comprehensive loss reflected on the balance sheet consists of the following (in thousands):

	April 30, 2002	January 31, 2002
Minimum pension liability adjustment	$ 5,799	$ 5,799
Adjustment to fair value of interest rate swaps	12,894	16,103
Accumulated comprehensive loss	$ 18,693	$ 21,902

Note 2. Goodwill

In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 142 provides that goodwill will no longer be amortized, but will instead be reviewed for impairment at least annually. SFAS 142 was effective for the Company on February 1, 2002.

As of February l, 2002, the Company had approximately $45.4 million of unamortized goodwill. Most of this total relates to the fiscal 2000 purchase of an additional ownership interest in the joint venture which operates MotorCity Casino. In accordance with SFAS 142, each property with assigned goodwill is to be valued as an operating entity. If the fair value of the operating entity is greater than the book value, including assigned goodwill, no further testing is required. However, if the book value, including goodwill, is greater than the fair value of the operating entity, the assets and liabilities of the operating entity need to be valued. The difference between the fair value of the operating entity and the fair value of the assets is the implied fair value of goodwill. To the extent that the implied fair value of goodwill is less than the book value of goodwill, an impairment charge will be recognized as a cumulative effect of a change in accounting principle upon adoption.

The Company has partially completed its implementation analysis of the goodwill arising from its prior acquisitions. For purposes of this analysis, the fair value of the operating entities was determined using a combination of a discounted cash flow model and a valuation multiple. Based upon this analysis, the Company recorded an impairment charge of $1.9 million, representing the goodwill associated with the June 1, 1995 acquisition of the Railroad Pass Hotel and Casino. This charge was reflected as a cumulative effect of a change in accounting principle in the quarter ended April 30, 2002. As permitted under SFAS 142, the Company is continuing its evaluation of $5.4 million of goodwill associated with the acquisition of the Edgewater Hotel and Casino. If the Company subsequently determines that an impairment exists, the amount would be reported as an adjustment to the previously reported cumulative effect of a change in accounting principle (as provided for in SFAS 142).

In the three months ended April 30, 2001, the Company recorded goodwill amortization of $3.0 million. Had the new rules been in effect for this prior period, the Company would have reported the following (in thousands):

		Three Months Ended April 30, 2001
Net income as reported	$	47,362
Add back: goodwill amortization		2,950
Adjusted net income	$	50,312
Net income per share as reported Basic	$	.62
Adjusted net income per share Basic	$	.66
Net income per share as reported Diluted	$	.61
Adjusted net income per share Diluted	$	.65

Note 3. Investments in Unconsolidated Affiliates

The Company has investments in unconsolidated affiliates that are accounted for under the equity method. Under the equity method, original investments are recorded at cost and adjusted by the Company's share of earnings, losses and distributions of these companies. The investment balance also includes interest capitalized during construction. Investments in unconsolidated affiliates consisted of the following (in thousands):

		April 30, 2002		January 31, 2002
Circus and Eldorado Joint Venture (50%) (Silver Legacy, Reno, Nevada)	$	53,925	$	77,029

	April 30, 2002	January 31, 2002
Elgin Riverboat Resort (50%) (Grand Victoria, Elgin, Illinois)	249,442	251,022
Victoria Partners (50%) (Monte Carlo, Las Vegas, Nevada)	226,435	226,035
	$ 529,802	$ 554,086

The Company's unconsolidated affiliates operate with fiscal years ending on December 31. Selected results of operations for each of the unconsolidated affiliates are as follows (in thousands):

March 31, 2002	Silver Legacy	Grand Victoria	Monte Carlo	Total
Revenues	$ 36,794	$ 104,884	$ 63,504	$ 205,182
Expenses	30,749	74,269	44,930	149,948
Operating income	6,045	30,615	18,574	55,234
Net income	3,412	30,814	18,037	52,263

March 31, 2001	Silver Legacy	Grand Victoria	Monte Carlo	Total
Revenues	$ 37,739	$ 101,502	$ 69,018	$ 208,259
Expenses	31,329	70,303	48,760	150,392
Operating income	6,410	31,199	20,258	57,867
Net income	2,429	31,778	18,783	52,990

Note 4. Long-term Debt

Long-term debt consisted of the following (in thousands):

	April 30, 2002	January 31, 2002
Amounts due under bank credit agreements at floating interest rates, weighted average of 3.8% and 3.6%	$ 300,000	$ 380,000
Amounts due under majority-owned joint venture revolving credit facility at floating interest rates, weighted average of 3.3%	46,000	64,000
6 3/4% Senior Subordinated Notes due 2003 (net of unamortized discount of $19 and $23)	149,981	149,977
9 1/4% Senior Subordinated Notes due 2005	275,000	275,000
6.45% Senior Notes due 2006 (net of unamortized discount of $165 and $176)	199,835	199,824
10 1/4% Senior Subordinated Notes due 2007	500,000	500,000
9 1/2% Senior Notes due 2008	200,000	200,000
9 3/8% Senior Subordinated Notes due 2010 (net of unamortized discount of $2,076 and $2,142)	297,924	297,858
7 5/8% Senior Subordinated Debentures due 2013	150,000	150,000
7.0% Debentures due 2036 (net of unamortized discount of $89 and $92)	149,911	149,908
6.70% Debentures due 2096 (net of unamortized discount of $76 and $88)	149,924	149,912
Other notes	4,760	4,859
	2,423,335	2,521,338
Less current portion	(36,251)	(39,251)

	April 30, 2002	January 31, 2002
	$ 2,387,084	$ 2,482,087

At April 30, 2002, the Company was in compliance with all of the covenants in its credit facilities and, under the most restrictive loan covenant, was restricted from issuing additional debt in excess of approximately $950 million.

Note 5. Interest Rate Swaps

The Company has a policy aimed at managing interest rate risk associated with its current and anticipated future borrowings. Under this policy, the Company may use any combination of interest rate swaps, futures, options, caps and similar instruments. To the extent the Company employs such financial instruments pursuant to this policy, and the instruments qualify for hedge accounting, they are accounted for as hedging instruments. In order to qualify for hedge accounting, the underlying hedged item must expose the Company to risks associated with market fluctuations and the financial instrument used must be designated as a hedge and must reduce the Company's exposure to market fluctuation throughout the hedge period. If these criteria are not met, a change in the market value of the financial instrument is recognized as a gain or loss in the period of change. Otherwise, gains and losses are not recognized except to the extent that the financial instrument is disposed of prior to maturity. Net interest paid or received pursuant to the financial instrument is included as interest expense in the period.

The Company has entered into various interest rate swaps, principally with its bank group, to manage interest expense, which is subject to fluctuation due to the variable-rate nature of the debt under the Company's credit facilities. The Company has interest rate swap agreements under which it pays a fixed interest rate (we